No. 85-1910-CFX
Status: GRANTED

Title: Business Electronics Corporation, Petitioner
v.
Sharp Electronics Corporation

Docketed:
May 21, 1986

Court: United States Court of Appeals
for the Fifth Circuit

Counsel for petitioner: McGowan,Gary V.

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Entry	Date	Note	Proceedings and Orders
1	May 21 1986	G	Petition for writ of certiorari filed.
2	Jun 19 1986		Brief of respondent Sharp Electronics Corp. in opposition filed.
3	Jun 24 1986		DISTRIBUTED. September 29, 1986
4	Jul 23 1986		REDISTRIBUTED. September 29, 1986
5	Oct 6 1986	P	The Solicitor General is invited to file a brief in this case expressing the views of the United States. Justice Scalia OUT.
6	May 13 1987		Brief amicus curiae of United States filed. VIDED.
7	May 18 1987		Supplemental brief of respondent /cross petitioner Sharp Electronics Corporation filed. VIDED.
8	May 19 1987		REDISTRIBUTED. June 4, 1987
9	Jun 2 1987	X	Supplemental brief of petitioner Business Electronics Corp. filed. VIDED.
10	Jun 8 1987		Petition GRANTED.
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11	Jun 22 1987		Record filed.
13	Jul 14 1987		Order extending time to file brief of petitioner on the merits until August 22, 1987.
14	Jul 23 1987		Joint appendix filed.
15	Aug 21 1987		Brief amici curiae of Forty-Two States filed.
16	Aug 21 1987		Brief amicus curiae of Natl. Mass Retailing Institute filed.
17	Aug 21 1987		Brief amicus curiae of K Mart Corporation filed.
18	Aug 22 1987		Brief of petitioner Business Electronics Corp. filed.
20	Sep 8 1987		Order extending time to file brief of respondent on the merits until October 21, 1987.
21	Oct 13 1987		Order further extending time to file brief of respondent on the merits until November 6, 1987.
22	Nov 6 1987		Brief amicus curiae of National Association of Manufacturers filed.
23	Nov 6 1987		Brief amicus curiae of Consumer Electronics Group of the Electronic Industries filed.
24	Nov 6 1987		Brief of respondent Sharp Electronics Corp. filed.
25	Nov 6 1987		Brief amicus curiae of National Office Machine Dealers Association filed.
26	Nov 23 1987		SET FOR ARGUMENT. Tuesday, January 19, 1988. (3rd case)
27	Dec 14 1987		CIRCULATED.
28	Jan 12 1988	X	Reply brief of petitioner Business Electronics Corp. filed.
29	Jan 12 1988		LODGING. (Report 100-421)
30	Jan 19 1988		ARGUED.

85-1910

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

NO. _____

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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I

QUESTION PRESENTED

The jury below found an agreement between the defendant supplier and a non-price cutting dealer to terminate a competing dealer for the purpose of eliminating price competition. On appeal, the defendant supplier did not contest the sufficiency of the evidence supporting this finding. Rather, the question presented here is whether dealer termination pursuant to a conspiracy to eliminate price competition constitutes price fixing in violation of the Sherman Act, absent an express finding of direct agreement on resale price levels.

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IN THE

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OCTOBER TERM, 1985

NO. _____

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The petitioner, Business Electronics Corporation, respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit entered in this proceeding on January 21, 1986.

OPINION BELOW

The opinion of the court of appeals is reported at 780 F.2d 1212 and appears in the Appendix hereto. The opinion of the district court denying defendant's motions for new trial and judgment n.o.v., which has not been reported, also appears in the Appendix hereto.

JURISDICTION

The judgment of the court of appeals was entered on January 21, 1986. A timely Suggestion for Rehearing En Banc was denied on February 20, 1986, and this Petition for Writ of Certiorari was filed within ninety (90) days of that date. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTE INVOLVED

Section 1 of the Sherman Act, 15 U.S.C. § 1, provides in pertinent part:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations is declared to be illegal. . . .

STATEMENT

1. From 1968 until July 1973, Business Electronics Corporation ("BEC"), owned and operated by Kelton Ehrensberger, was an authorized dealer in Sharp brand electronic calculators in Houston. As such, BEC bought calculators from Sharp Electronics Corporation ("Sharp") and resold them at retail.

Although Sharp suggested resale prices to its dealers and authorized specific discounts from list prices for

certain accounts, BEC frequently sold at lower prices/greater discounts than those authorized by Sharp. Consequently, Sharp's Texas representative, Mr. Burkholder, complained to BEC about this price cutting, noting that BEC was "messing up" the market and "creating dealer complaints." Tr. 73-77, 239-40, 244, PX 52.* When BEC encountered problems in obtaining prompt delivery of preferred models in sufficient quantity, Burkholder said that Sharp was in a position to make inventory problems very "painful" for BEC if it continued to price the machines "arbitrarily." Tr. 79-80.

In mid-1972, Sharp threatened cancellation of BEC's dealership. At this time, Hiroshi Kawai, Sharp's Vice President, told Ehrensberger that he should "clean up his pricing structure." Tr. 81. Almost contemporaneously, Sharp appointed an additional dealer in Houston—Hartwell's Office World, owned and operated by Gil Hartwell. Hartwell soon began a campaign to stop BEC's price cutting. Tr. 174-75. In a July 1972 letter to Ehrensberger, copied to Burkholder, Hartwell wrote that he would not "compete" with BEC for a particular customer "so the customer won't be able to play one of us against the other in a 'discount' situation." Tr. 84-85, PX 40. Regarding this letter, Hartwell testified that he "was making the first step to lending some price stability to Mr. Ehrensberger" and that he intended to charge Sharp's suggested list prices. Tr. 276-77. Hartwell further testified that Ehrensberger was discounting from Sharp's suggested list price and that Hartwell wanted to avoid that. Tr. 278.

Hartwell thereafter complained to Sharp, including Burkholder, Tom Mashos (National Sales Manager),

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* "Tr." refers to the official transcript of the trial record below. "PX" refers to plaintiff's exhibits admitted into evidence below.

and Kawai, about BEC's price cutting, which Hartwell wanted stopped. Tr. 79, 280, 283, 287, 837. Kawai relayed these complaints back to Burkholder and told him to "try to solve the problem." Tr. 628, 629, 636, 639. In October 1972, Burkholder wrote Kawai about "problems created by Ehrensberger," meaning the Hartwell complaints concerning BEC's price-cutting. Tr. 933-34. In December 1972, Hartwell wrote to Kawai complaining again about BEC's "price cutting," PX 39, Tr. 88-90, which he wanted Kawai to correct. Tr. 286. Subsequently, Burkholder told Ehrensberger that he wanted BEC "to maintain the correct discount range." Tr. 91.

In mid-1973, Hartwell did more than complain. He demanded that Sharp terminate BEC for the *express* purpose of stopping the discounting. Hartwell delivered an "ultimatum" to Mashos—because of BEC's price cutting, Hartwell would quit unless Sharp canceled BEC. Within three weeks, Mashos complied with this demand and terminated BEC. Tr. 189-90, 586, 587, 1355-56. Thereafter, Hartwell remained as Sharp's Houston dealer. Tr. 294.

Hartwell's policy was to sell at Sharp's suggested list prices, and he usually adhered to those prices in the years following BEC's termination. Tr. 294-95, 296, 398. Accordingly, Hartwell's gross margin—the difference between his cost of purchasing the product from Sharp and his resail price—increased after BEC was terminated.*

BEC brought this suit under § 1 the Sherman Act, contending that Sharp and Hartwell conspired to terminate BEC for the purpose of eliminating price competition.

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* Hartwell's gross margin increased from 33% in 1972 and 34% in 1973 to 43% in 1974 and 45% in 1975. PX 119, Tr. 1156, 389-91.

2. The district court submitted the following liability interrogatory to the jury:

> Question 1: Do you find by a preponderance of the evidence that there was an agreement or understanding between Sharp and Hartwell to terminate Business Electronics because of Business Electronics' price cutting?

The court instructed the jury that the plaintiff "must show . . . that Sharp and Hartwell knowingly came to a common and mutual understanding to accomplish or attempt to accomplish an unlawful purpose. . . ." Tr. 1584. The court further instructed:

> Plaintiff contends that Sharp terminated Business Electronics in furtherance of Hartwell's desire to eliminate Business Electronics as a price cutting rival. . . . If you find that Sharp did not terminate Business Electronics pursuant to an *agreement . . . with Hartwell to eliminate price-cutting* by Business Electronics, then you should answer 'No' to question No. 1.

Tr. 1587 (emphasis added).

The jury answered Question number 1 affirmatively, found that the conspiracy had injured BEC, and awarded $600,000 in damages. Pursuant to 15 U.S.C. § 4, the district court entered judgment for BEC for treble this amount plus attorneys fees.

After the district court denied Sharp's motions for judgment n.o.v. and for new trial, Sharp appealed to the United States Court of Appeals for the Fifth Circuit.

3. The Fifth Circuit reversed the judgment below and remanded for retrial. Acknowledging that several other

circuits have adopted the standard of liability embodied in the district court's instructions, the court nevertheless rejected the rule that termination of a price-cutting dealer pursuant to a conspiracy to eliminate price competition constitutes unlawful price fixing. According to the Fifth Circuit, unlawful price fixing requires proof of an agreement "to set prices at some level, though not a specific one." 780 F.2d at 1218. Because the jury instructions did not reflect this liability standard, the court found them defective.

Nevertheless, the court held that the evidence was sufficient to support a jury finding that "Sharp and Hartwell reached an agreement as to price." *Id.* at 1219. The court suggested that on remand the district court should ask the jury whether Sharp's decision to terminate BEC was made pursuant to a conspiracy with Hartwell to "fix, maintain or stabilize" resale prices of Sharp electronic calculators. *See id.* at 1218 n.3.

REASONS FOR GRANTING THE PETITION

This appeal concerns a vital but discrete issue of federal antitrust law: whether an agreement between a manufacturer and a dealer to terminate a competing dealer for the purpose of eliminating price competition constitutes a violation of § 1 of the Sherman Act. It is important to recognize what is *not* at issue here. There is no issue whether Sharp and Hartwell agreed to terminate BEC for a price-related reason or whether the evidence satisfied the standard for proving collusion set forth in *Monsanto Co. v. Spray-Rite Service Corp.*, 104 S. Ct. 1464 (1984). There also is no issue as to the sufficiency of the evidence to support a finding of unlawful price fixing even under the standard articulated by the Fifth Circuit. *See* 780 F.2d at 1219.

At trial below, the jury found that Sharp terminated BEC pursuant to an agreement with Hartwell to eliminate price competition. According to the Fifth Circuit, such an agreement falls short of price fixing because it does not directly fix prices. In the Fifth Circuit's view, an agreement to eliminate price competition is not unlawful unless the conspirators also agreed directly "to set resale prices at some level. . . ." 780 F.2d at 1218. As demonstrated herein, imposition of this requirement contravenes the established definition of price fixing adopted by this Court and followed by the federal courts for forty-five years. The Fifth Circuit is the only federal court to adopt this standard, which, by its own admission, places antitrust law in the Fifth Circuit in direct conflict with the law in four sister circuits.

Even worse, the decision below creates a significant loophole in the established antitrust policy against price fixing. By requiring proof of a direct agreement on resale prices, the Fifth Circuit has imposed the near impossible task of proving that manufacturer and competing dealer literally agreed to "fix" retail prices "at some level. . . ." As a result, in the Fifth Circuit, manufacturers will be free to serve as price "policemen" for dealers who want to stop discounting by other dealers. Recognizing the anticompetitive consequences of such conduct, Congress, in recent legislation signed by the President, expressly stated its view that resale price fixing does not require proof of agreement on specific prices. *See* Pub. L. No. 99-180 at § 605, 99 Stat. 1136, 1169-70 (Dec. 13, 1985).

In view of the critical importance of the antitrust prohibition against price fixing, this Court should hear this case to consider the Fifth Circuit's unprecedented and fundamentally erroneous departure from established law.

1. Decisions Of This Court Firmly Establish That An Agreement To Eliminate Price Competition Constitutes Unlawful Price Fixing.

The Fifth Circuit's decision conflicts with decisions of this Court. Long ago, this Court broadly defined illegal price fixing as "a combination formed for the purpose or with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity. . . ." *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 223 (1940). As more recently stated by the Court: "Price is the 'central nervous system of the economy,' . . . and an agreement that 'interfere[s] with the setting of price by free market forces' is illegal on its face. . . ." *National Society of Professional Engineers v. United States*, 435 U.S. 679, 692 (1978).

No federal court has ever before required proof of an agreement "to set prices at some level" as an essential element of price fixing. Indeed, in the seminal *Socony-Vacuum* case, this Court held that the offense of price fixing does not entail prices "fixed in the sense that they were uniform and inflexible. Price-fixing . . . has no such limited meaning." 310 U.S. at 222. Applying this long established concept, this Court recently held that an agreement to eliminate credit terms was "tantamount to an *agreement to eliminate discounting*, and thus [fell] squarely within the traditional *per se* rule against price fixing." *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 648 (1980) (emphasis added). In *Catalano*, the Court said:

> In . . . *Socony-Vacuum* . . . we held that a program of buying surplus gasoline on the spot market in order to prevent prices from falling sharply was unlawful without any inquiry into the reasonableness of the program, *even though there was no direct agreement on the actual prices to be maintained*. . . .
>
> Thus we have held agreements to be unlawful per se that had substantially less direct impact than the agreement in this case.

Id. at 647 (emphasis added). The Court further noted that the agreement at issue was "merely one form of price fixing." *Id.* at 650; *accord, United States v. Gasoline Retailers Association*, 285 F.2d 688 (7th Cir. 1961) (agreement not to advertise price is per se illegal price fixing even without direct agreement on price).

Similarly, this Court's decision in *United States v. General Motors Corp.*, 384 U.S. 127, 145-48 (1966), squarely rejected the notion that an agreement to eliminate discounters was somehow less pernicious than a direct agreement to fix prices. Holding that a conspiracy to eliminate discounters was a per se violation of the Sherman Act, the Court reasoned:

> The protection of price competition from conspiratorial restraint is an object of special solicitude under the antitrust laws. We cannot respect that solicitude by closing our eyes to the effect upon price competition of the removal from the market, by combination or conspiracy, of a class of traders. Nor do we propose to construe the Sherman Act to prohibit conspiracies to fix prices at which com-

petitors may sell, but to allow conspiracies or combinations to put competitors out of business entirely.

Id. at 148; *contra, St. Petersburgh Yacht Charters, Inc. v. Morgan Yacht, Inc.*, 457 So.2d 1028 (Fla. Dist. Ct. App. 1984) (sole authority cited by decision below).

Even though the above cases dealt with horizontal price-fixing conspiracies, their holdings are not limited to the horizontal context. In condemning vertical price restraints, this Court has often cited the same broad description of price fixing set out in *Socony*. *See, e.g., Simpson v. Union Oil Co.*, 377 U.S. 13, 18 (1964); *United States v. Parke, Davis and Co.*, 362 U.S. 29, 47 (1960). Logically, an agreement intended to eliminate discounting amounts to price fixing by this definition whether it is vertical or horizontal in nature.

In this regard, the Court held in *Parke, Davis* that direct agreement on resale prices is not a required element of unlawful price fixing. There, a manufacturer refused to deal with wholesalers who charged less than suggested resale prices and enlisted the cooperation of wholesalers in cutting off offending retailers. Even though there was no direct agreement on price, the Court held that the scheme constituted illegal price fixing. The Court said: "[A]n unlawful combination is *not* just such as arises from a price maintenance *agreement*, express or implied; such a combination is *also* organized if the producer secures adherence to his suggested prices by means which go beyond his mere declination to sell to a customer who will not observe his announced policy." 362 U.S. at 43 (emphasis added in part).

The agreement between Sharp and Hartwell, although vertical in nature, stifled horizontal competition in both

purpose and effect. Having failed to enlist BEC in a horizontal conspiracy to fix prices, Hartwell engaged Sharp to accomplish the same purpose and result by vertical conspiracy. As stated in *General Motors*, the courts should not close their eyes to "the effect upon price competition of the removal from the market, by combination or conspiracy, of a class of traders." 384 U.S. at 148. Whether in the vertical context or the horizontal context, it would not make sense "to construe the Sherman Act to prohibit conspiracies to fix prices at which competitors may sell, but to allow conspiracies or combinations to put competitors out of business entirely." *Id.*

Even if the agreement between Sharp and Hartwell did not directly "fix" prices "at some level," it was clearly intended to destroy price competition in a most effective way—removal of a competitor *because* he refused to honor his competitor's demands for compliance with Sharp's suggested resale prices. Unquestionably, this conspiracy to eliminate price competition, in the words of this Court, "falls squarely within the traditional *per se* rule against price fixing" and is "merely a form of price fixing." 446 U.S. at 648, 650.

2. In Direct Conflict With The Decision Below, At Least Four Other Courts Of Appeals Have Held That Price Fixing Occurs When A Supplier Terminates A Dealer Pursuant To a Conspiracy With A Competing Dealer To Eliminate Price Competition.

The Fifth Circuit acknowledged that its holding in this case directly conflicts with the holdings of four other circuit courts of appeals:

> We recognize that the standard of liability we set forth conflicts with the rule enunciated in *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 170 (3d Cir. 1979) and followed by a number of other circuits.

780 F.2d at 1216. Indeed, every other federal court to consider this question has held that unlawful price fixing occurs when a supplier terminates a dealer pursuant to a conspiracy with a competing dealer to eliminate price competition—the precise jury finding in the instant case. *See Victorian House, Inc. v. Fisher Camuto Corp.*, 769 F.2d 466 (8th Cir. 1985); *Ziddell Exploration, Inc. v. Conval International, Ltd.*, 719 F.2d 1465, 1469 (9th Cir. 1983); *Roesch, Inc. v. Star Cooler Corp.*, 712 F.2d 1235, 1237 (8th Cir. 1983) (en banc), *cert. denied*, 104 S. Ct. 1707 (1984); *Spray-Rite Service Corp. v. Monsanto Co.*, 684 F.2d 1226, 1234 (7th Cir. 1982), *aff'd on other grounds*, 104 S. Ct. 1464 (1984); *Contractor Utility Sales Co. v. Certain-Teed Products Corp.*, 638 F.2d 1061, 1072 (7th Cir. 1981); *Alloy International Co. v. Hoover-NSK Bearing Co.*, 595 F.2d 164, 170 (3d Cir. 1979); *Girardi v. Gates Rubber Co. Sales Division, Inc.*, 325 F.2d 196, 200 (9th Cir. 1963); *see also Trabert & Hoeffler, Inc. v. Piaget Watch Corp.*, 633 F.2d 477 (7th Cir. 1980). The Ninth Circuit's holding in *Ziddell* sharply illustrates this conflict:

> [I]f a manufacturer withdraws its product from a price-cutting distributor at the request of a competing distributor as part of a conspiracy to protect the requesting distributor from price competition, the manufacturer has committed a per se violation of the antitrust laws.

719 F.2d at 1469.

The impact of this conflict is substantial, encompassing all businesses operating in or substantially affecting interstate commerce and subject to the Sherman Act. Uniform interpretation of the issue of law involved—the standard of liability for unlawful price fixing—clearly is vital to efficient business planning at all levels of the chain of distribution. There can be no justification for deciding claims of unlawful price fixing based upon standards of liability which materially differ depending upon the geography of the place of suit.

3. The Decision Below Creats An Unprecedented, Substantial Loophole in the Important Federal Prohibition Against Price Fixing.

Recognizing the direct conflict with the rule accepted in other circuits, and citing no federal case directly announcing a contrary rule, the Fifth Circuit based its holding on inapplicable cases and reasoning that misapprehends the conspiracy found by the jury. No federal court has *ever* held that termination of a dealer pursuant to an agreement to eliminate price competition is anything except an illegal price restraint. The *only* case directly supporting the panel's view is an opinion of a state appellate court in Florida, which is contrary to Supreme Court precedent construing the Sherman Act. *Compare General Motors Corp.*, 384 U.S. at 148, *with St. Petersburgh Yacht Charters*, 1984-1 Trade Cas. at p. 68,337.

There are at least four basic mistakes in the Fifth Circuit's analysis of vertical price fixing. We address them in turn.

a. The Fifth Circuit reasoned that "an agreement to terminate a price cutter does not fix prices at any specific or general level but merely frees the complaining dealer to set prices he chooses." 780 F.2d at 1216. Under comparable reasoning, a bank robber is "free" to return stolen money to the bank, and an agreement to terminate an employee for union membership "frees" the remaining employees to organize, or not, as they choose. Collusive elimination of a discounting dealer may theoretically "free" the complaining dealer to set prices as he chooses, but it takes little imagination to conclude that the dealer will use his new-found "freedom" from price competition to increase price or avoid discounting. After all, it was price cutting which prompted his complaints in the first place. Moreover, other dealers will have been disciplined by example not to offer discounts from stabilized or enhanced price levels. With due respect, the obvious and only purpose of dealer termination pursuant to agreement to eliminate price cutting is, *ipso facto,* to raise, maintain, or stabilize prices.

Permitting a dealer to use a manufacturer as his agent to eliminate a competitor who refuses to fix prices poses dangers to price competition equal to those created by a cartel between the two dealers themselves. Contrary to the reasoning below, the manifiestly anticompetitive effects of an agreement to eliminate price competition are not offset by the absence of a complementary agreement to set prices "at some level." Therein lies the real danger in the court's decision—the creation of a gaping loophole through which a destructive form of price fixing will escape liability under the antitrust laws. Now, in the

Fifth Circuit, a dealer may obtain a manufacturer's agreement to police discounting by other dealers so long as the manufacturer and dealer do not directly agree on "some price level."

b. The court characterized the agreement at issue as similar to the grant of an exclusive distributorship, which, though it may have the effect of raising prices, is not illegal per se. *Id.* But the evidence here demonstrated, and the jury found, *more* than a mere exclusive distributorship agreement which might incidentally affect prices. The district court instructed the jury that it could find an unlawful conspiracy *only* if Sharp terminated BEC "pursuant to an agreement . . . with Hartwell *to eliminate price-cutting* by BEC. . . ." Tr. at 1587. Lawful exclusive distributor agreements do not contemplate this element. Clearly, the grant of an exclusive distributorship on the condition that the distributor not engage in price cutting would itself be illegal per se.

c. The court erroneously relied on cases addressing unilateral dealer termination or nonprice restraints. For instance, the court plainly misread its own decision in *Aladdin Oil Co. v. Texaco, Inc.,* 603 F.2d 1107 (5th Cir. 1979). Focusing narrowly on a passage in *Aladdin* saying that "abstract lessening of competition is not enough" to prove an antitrust violation, *id.* at 1116, the court concluded that *Aladdin* "demonstrates both the error committed in this case and the proper standard of liability." 780 F.2d at 1215. Read in context, however, the *Aladdin* passage concerned refusals to deal which are *not* price-related. Moreover, elimination of price cutting is more than mere "abstract lessening of intrabrand competition." *Ron Tonkin Gran Turismo v. Fiat Distributors,* 637 F.2d 1376, 1388 n.12 (9th Cir.), *cert. denied,* 454 U.S. 831 (1981).

d. Although acknowledging that *Monsanto Co. v. Spray-Rite Service Corp.*, 104 S. Ct. 1464 (1984), "did not expressly disapprove" the rule embodied in the jury instructions below, 780 F.2d at 1218, the Fifth Circuit nevertheless extrapolated the *Monsanto* holding beyond its intended limit. In *Monsanto,* this Court held that concert of action cannot be inferred from mere evidence of dealer pricing complaints followed by termination in response to those complaints. The Court found such evidence to be "highly ambiguous," since it does not exclude the possibility that the manufacturer unilaterally decided to terminate. Thus, *Monsanto* requires the plaintiff to adduce additional "evidence that tends to exclude the possibility that the manfacturer and non-terminated distributor were acting independently." 104 S. Ct. at 1471. Going far beyond this holding, the Fifth Circuit concluded that even an actual *agreement* to terminate because of price cutting does not constitute price fixing, since, the court reasoned, only a "mind reader" could distinguish between such an agreement and unilateral termination in response to dealer complaints. 780 F.2d at 1218. The court's reasoning will not withstand analysis.

First, *Monsanto* dealt only with the minimum proof required to show concert of action. Here, Sharp has never contested the sufficiency of evidence supporting the jury finding of concerted agreement. Rather, Sharp contended only that the agreement found by the jury did not constitute price fixing. Second, unlike mere evidence of complaints followed by termination, an agreement to terminate because of price cutting, as specifically found by the jury below, is by definition entirely free of ambiguity on the question of collusion. Third, the instructions below required the jury to determine, not merely whether Hartwell complained and Sharp terminated, but whether the

termination was done "pursuant to an agreement . . . to eliminate price cutting by [BEC] . . . ." Tr. 1587. Fourth, the evidence in this case of an agreement to terminate because of price cutting was far greater than mere evidence of termination in response to dealer complaints. The Fifth Circuit itself said:

> There is evidence that, even before Hartwell became a dealer, Sharp sought BEC's adherence to the suggested retail price list. BEC produced evidence tending to show that it was not "free-riding" and that its sales performance was equal to Hartwell's. The logical inferences from such evidence, if drawn by the jury, could support a finding that BEC's termination was not due to the reasons Sharp suggests. . . .
>
> In addition, there was evidence that Hartwell usually followed Sharp's suggested prices. There was also evidence that Hartwell sought to encourage BEC to follow these prices. Finally, the record shows that Hartwell complained vigorously to Sharp about BEC's pricing and that ultimately Sharp responded by terminating BEC. This evidence, taken as a whole and viewed in the light most favorable to BEC, could support an inference that Sharp and Hartwell had agreed that Hartwell would follow Sharp's suggested retail prices and that BEC's termination was pursuant to this agreement.

780 F.2d at 1219. This evidence, along with Hartwell's express demand that Sharp terminate BEC for price cutting, satisfies the *Monsanto* requirement of "evidence which tends to exclude the possibility that the manufacture and non-terminated distributor were acting independently," and removes this case from the mere "termination-in-response-to-complaints" category. The only issue

here is whether an agreement to eliminate price cutting is different *in substance* from a "price maintenance agreement." They are the same, and to hold otherwise is to glorify semantics and ignore the substance of the agreement at issue.

4. The Decision Below Contravenes Congressional Intent.

Congress recently passed legislation that implicitly rejects the holding below. See Pub. L. 99-180 at § 605, 99 Stat. 1136, 1169-70 (Dec. 13, 1985). As a prelude to this legislation, the House of Representatives issued House Report 99-399 on November 21, 1985. H.R. 99-399, which stongly criticizes the so-called "Vertical Restraints Guidelines" published by the Department of Justice in January 1985,* says in part:

> Other "restatements" of the law exist in the Guidelines that attempt to dilute or trivialize the generality of the per se rule against price fixing, both horizontal and vertical. *The Division claims,* again without accompanying authorities, *that vertical price fixing is lawful so long as the agreement to fix prices does not set "specific" resale prices* and is ancillary to one or more non-price restraints. . . . Such a statement appears to reject or ignore any consideration of the effects of a restraint on price in determining whether there is a price fixing agreement.
>
> * * * * *
>
> In all these respects, the Guidelines are *inconsistent with existing law* and are also demonstrably *unsound as a matter of policy*.

* Sharp expressly relied on these Guidelines in its brief filed in the Fifth Circuit below.

(Emphasis added). This Report led to Congressional enactment of § 605 of Pub. L. 99-180 which reads in pertinent part:

> Whereas such ["Vertical Restraint Guidelines" published by the Justice Department] are inconsistent with established antitrust law . . . in stating that vertical restraints that have an impact upon prices are subject to the per se rule of illegality only if there is an *'explicit agreement as to the specific prices'* . . . ;
>
> * * * * *
>
> . . . Now, therefore, be it
>
> *Resolved,* That it is the sense of the Congress that the antitrust enforcement policy guidelines stated in "Vertical Restraints Guidelines" . . .
>
> are *not an accurate expression of the Federal antitrust laws or congressional intent with regard to the application of such laws to resale price maintenance.* . . .

99 Stat. at 1169-70 (emphasis added in part).

This statement of Congressional intent pinpoints the critical flaw in the decision below: the notion that the per se rule against price fixing narrowly applies only to direct agreements on resale price levels. The Congress recognized that, in substance, both concerted elimination of price cutting and direct agreement on price are forms of price fixing having the same illicit purpose and effect.

CONCLUSION

This Court observed only a few weeks ago:

> . . . [C]utting price in order to increase business often is the very essence of competition.

Matsushita Electric Industrial Co. v. Zenith Radio Corp., No. 83-2004, slip op. at 19 (U.S. March 26, 1986). By holding that a conspiracy to eliminate price competition does not amount to unlawful price fixing, the Fifth Circuit struck a blow to the heart of federal antitrust policy—the preservation of price competition. If the decision below is allowed to stand, manufacturers in the Fifth Circuit may obtain from their dealers an agreement not to compete on price without fear of per se liability.

For the reasons stated above, a writ of certiorari should be issued to review this erroneous evisceration of the doctrine against price fixing.

Respectfully submitted,

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Dated: May 20, 1986.

CERTIFICATE OF SERVICE

This is to certify that three true and correct copies of the foregoing Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit by Petitioner Business Electronics Corporation were served by mail on counsel of record for Respondent on the 20th day of May, 1986.

_____
GARY V. MCGOWAN

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

NO. 84-2618

BUSINESS ELECTRONICS CORPORATION,
Plaintiff-Appellee,

v.

SHARP ELECTRONICS CORPORATION,
Defendant-Appellant.

(Filed January 21, 1986)

OPINION

Before: Charles Clark, Chief Judge, Homer Thornberry, and Edith H. Jones, Circuit Judges.

Opinion by Judge Charles Clark;
Concurrence by Judge Edith H. Jones

Appeal from the United States District Court
for the Southern District of Texas

Woodrow Seals, Senior District Judge, Presiding

SUMMARY

Antitrust/Evidence

Appeal from verdict in favor of Business Electronics Corporation (BEC). Reversed and remanded.

BEC was Sharp Electronics Corporation's (Sharp's) sole electronic calculator dealer in the Houston area.

BEC often sold Sharp's products below the retail list price. Sharp became dissatisfied with BEC and appointed Hartwell as a dealer in the same area. Hartwell complained about BEC's pricing policies and eventually told Sharp that either BEC must be terminated or he would terminate his Sharp dealership. Sharp terminated BEC. BEC sued under the Sherman Act and the case was submitted to the jury on the theory that an agreement between Sharp and Hartwell to terminate BEC because of the latter's price cutting constitutes a per se violation of section one of the Sherman Act.

[1] It was not enough for the jury to find that BEC was terminated to reduce price competition; the jury should have been required to find that the termination was pursuant to a price maintenance agreement between Sharp and Hartwell. [2] It is recognized that this conflicts with the rule followed by other circuits that if a manufacturer deliberately withdraws its product from a price-cutting distributor at the request of a competing distributor as part of a conspiracy to protect the requesting distributor from price competition, the manufacturer has committed a per se violation of the antitrust laws. [3] That rule is not adopted in the Fifth Circuit. Any vertical non-price restriction may affect resale prices, yet the Supreme Court has held such restrictions are nonetheless to be evaluated under the rule of reason. [4] This position is supported by *Monsanto Co. v. Spray-Rite Service Corp.*, ____U.S.____, 104 S. Ct. 1464, ____L.Ed.2d____, *reh'g denied*, 104 S. Ct. 2378 (1984) which drew distinctions between concerted and independent action (only the former is proscribed by the Sherman Act) and [5] between concerted action to set prices and concerted action on non-price restrictions (the former is illegal per se

while the latter is evaluated under the rule of reason). [6] It is possible to interpret *Monsanto* as saying merely that a manufacturer can terminate a price cutter whether or not a complaining dealer "agrees" as long as the manufacturer is acting for some reason other than just knuckling under to the complaining dealer's desire for less competition. However, this would lead to the very "irrational dislocations" *Monsanto* sought to avoid. [7] In order for a manufacturer's termination of a distributor to be illegal per se, it must be pursuant to a price maintenance agreement with another distributor. The jury instructions in this case failed to reflect this standard and were, therefore, critically defective.

[8] To grant the relief requested by Sharp, reversal of the denial of its motions for directed verdict and for judgment notwithstanding the verdict and dismissal of the complaint, it is necessary to determine that the evidence is such that reasonable men could arrive at only one verdict. [9] However, the evidence was sufficient to support a properly directed jury verdict in BEC's favor.

[10] A document Sharp sought to introduce should not have been excluded on hearsay grounds. Sharp was not offering the document to prove the truth of the statements therein. It was offered to show Sharp believed BEC had only made 45% of its sales quota. [11] Likewise, documents received by Sharp's Texas representative setting quotas and emphasizing the importance of meeting quotas were admissible to show the representative was under pressure to meet quotas.

[12] An antitrust plaintiff is not required to prove with exact particularity what its success might have been in the market absent the illegal conduct of another. There-

fore, Hartwell's sales could have been used as a yardstick to measure BEC's damages as he sold the same product in the same area.

The concurrence stated that this case perfectly illustrates the argument why vertical price restraints should be tested under anti-trust's rule of reason rather than, as *Monsanto* continues to require, per se illegality.

OPINION

CHARLES CLARK, Chief Judge:

Defendant-appellant Sharp Electronics Corporation (Sharp) appeals from a jury verdict in favor of plaintiff-appellee Business Electronics Corporation (BEC), a former dealer in Sharp calculators, on BEC's claim that Sharp committed a *per se* violation of section one of the Sherman Act by agreeing with a competing dealer to terminate BEC because of its price cutting. Sharp contends that (1) the district court erred in instructing that it must find *per se* liability without regard to any agreement on price, (2) the evidence was insufficient to support a jury finding of *per se* liability, (3) there should be no rule of *per se* liability in vertical price fixing cases, (4) the district court committed prejudicial error in making certain evidentiary rulings and (5) the district court accepted an erroneous measure of damages. Because the jury was improperly instructed on point (1), we reverse and remand for a new trial.

I

Sharp is a supplier of various consumer and business products, including electronic calculators, throughout the

United States. Sharp distributed its calculators through a network of retail dealers that bought the calculators from Sharp and resold them to end users. Sharp provided retail price lists which suggested resale prices to its dealers.

In 1968, Sharp appointed Kelton Ehrensberger as its sole electronic calculator dealer in the Houston area. Ehrensberger later incorporated as BEC and continued his dealership under that name. BEC's sales strategy involved keeping retail prices low and BEC often sold at prices lower than those on Sharp's retail price lists.

It is apparent that, several years after Ehrensberger became a Sharp calculator dealer, Sharp became dissatisfied with BEC's performance. The parties disagree, however, on the reason for Sharp's dissatisfaction. Sharp presented evidence that BEC failed to meet sales quotas and that Sharp remonstrated with it for this poor sales performance. BEC, on the other hand, presented evidence that Sharp was concerned about BEC's discounting and wanted BEC to "clean up [its] pricing structure."

In mid-1972, Sharp's problem with BEC led to the appointment of Gilbert Hartwell as a Sharp calculator dealer in the Houston area. The record indicates that Sharp may have initially promised Hartwell that his dealership would be exclusive, but Sharp subsequently decided to retain BEC until more was learned about the market.

Hartwell was very upset about BEC's pricing policies and suggested to Ehrensberger that the dealers avoid a "discount" situation. He also complained bitterly to Sharp that BEC was undercutting him in the market. There was evidence that Sharp shared Hartwell's concern, although Hartwell testified that Sharp consistently told him that

it could not tell BEC what prices to charge. Hartwell also testified that he was not concerned about BEC's price cutting in general but only about BEC's "free riding" on Hartwell's investment in product promotion and other sales-related services. He stated that the customers which he developed through these means would then buy from BEC at lower prices.

In June, 1973, Hartwell presented an ultimatum to Sharp—unless Sharp terminated BEC within 30 days, Hartwell would terminate his own Sharp dealership. Sharp responded by terminating BEC.

The evidence showed that Hartwell usually, but not always, adhered to Sharp's suggested retail prices. According to Hartwell's testimony, he was under no obligation to sell at any particular price. The prices of Sharp calculators have dropped since 1973.

II

The district court submitted this case to the jury on the theory that an agreement between Sharp and Hartwell to terminate BEC because of the latter's price cutting constitutes a *per se* violation of section one of the Sherman Act. The district court charged the jury:

> The Sherman Act is violated when a seller enters into an agreement or understanding with one of its dealers to terminate another dealer because of the other dealer's price cutting. Plaintiff contends that Sharp terminated Business Electronics in furtherance of Hartwell's desire to eliminate Business Electronics as a price-cutting rival.

The court also submitted a special interrogatory to the jury, which it described as follows:

> Question number 1 asks you whether you find by a preponderance of the evidence that there was an agreement or understanding between Sharp and Hartwell to terminate Business Electronics as a Sharp dealer because of Business Electronics' price-cutting.

This theory, which does not require an agreement between Sharp and Hartwell to maintain resale prices, is an incorrect one. This court's decision in *Aladdin Oil Co. v. Texaco, Inc.*, 603 F.2d 1107 (5th Cir. 1979), demonstrates both the error committed in this case and the proper standard of liability. In *Aladdin Oil,* the plaintiff sought to acquire the assets of a Texaco distributorship which was going out of business. However, defendant Texaco, the supplier of oil and gasoline products, consulted with defendant Powertram, the other Texaco distributor in the area, and decided that Texaco did not need two distributors in the same area. Therefore, Texaco, which had an option to purchase the failing distributorship, decided to assign its option to Powertram and prevent the plaintiff from acquiring a distributorship in competition with Powertram. This court held that this conduct alone did not violate the antitrust laws. The fact that plaintiff alleged that Texaco and Powertram had prevented it from acquiring a distributorship in order to lessen intrabrand competition made no difference because "abstract lessening of intrabrand competition is not enough." *Id.* at 1116. The court indicated, however, that had Texaco's action been taken pursuant to a price maintenance agreement with Powertram, it would have violated the antitrust laws. *Id.* at 1117.

[1] Similarly, in the present case it was not enough for the jury to find that BEC was terminated to reduce price competition; the jury should have been required to

find that the termination was pursuant to a price maintenance agreement between Sharp and Hartwell. *St. Petersburg Yacht Charters, Inc. v. Morgan Yacht, Inc.*, 457 So.2d 1028, 1050 (Fla. Dist. Ct. App. 1984); *see also Borger v. Yamaha Int'l Corp.*, 625 F.2d 390, 397 (2d Cir. 1980) (improper for jury instructions to state that a dealer termination was unlawful "solely on the basis of a purpose to restrict intrabrand competition"). Additional support for this proposition may be found in *Muenster Butane, Inc. v. Stewart Co.*, 651 F.2d 292, 294-95 (5th Cir. 1981), where the court treated the termination of a dealer, apparently to protect another dealer from "intense competitive pricing," as a vertical non-price restraint to be tested under the rule of reason. *See also Joe Regueira, Inc. v. American Distilling Co., Inc.*, 642 F.2d 826, 833 (5th Cir. 1981) (plaintiff was required to show that its termination "was the result of a combination . . .which had as its purpose or effect the *fixing* of wholesale and retail prices") (emphasis added). An example of the type of instruction that would have been proper in this case may be found in *Pierce v. Ramsey Winch Co.*, 753 F.2d 416, 428 n.14 (5th Cir. 1985).

[2] We recognize that the standard of liability we set forth conflicts with the rule enunciated in *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 170 (3d Cir. 1979) and followed by a number of other circuits. *E.g., Victorian House, Inc. v. Fisher Camuto Corp.*, 1985-2 Trade Cases ¶ 66,706 at 63,382 (8th Cir. July 18, 1985); *Zidell Exploration, Inc. v. Conval Int'l, Ltd.*, 719 F.2d 1465, 1469 (9th Cir. 1983); *Bostick Oil Co. v. Michelin Tire Corp.*, 702 F.2d 1207, 1215 (4th Cir.), *cert. denied*, ____U.S.____, 104 S. Ct. 242 (1983). The *Cernuto* rule is that "if a manufacturer deliberately withdraws its product from a price-cutting distributor at the request of a competing distributor as part of a conspiracy to protect the requesting distributor from price competition, the manufacturer has committed a per se violation of the antitrust laws." *Zidell, supra,* 719 F.2d at 1469. The courts following this rule reason that if the manufacturer and dealer wish to protect the dealer from price competition then they must intend that prices be higher once the price-cutting dealer is terminated.

[3] This circuit has not adopted this reasoning. *See St. Petersburg Yacht Charters, supra,* 457 So.2d at 1048-49 (citing *Muenster Butane, Inc., supra,* 651 F.2d at 294-95). An agreement to terminate a price cutter does not fix prices at any specific or general level but merely frees the complaining dealer to set prices as he chooses. *St. Petersburg Yacht Charters, supra,* 457 So.2d at 1043-45. It is true that the effect of terminating the price cutter may be to raise prices but this is equally true of the granting of an exclusive dealership, which we have held not to be *per se* illegal. *Carlson Machine Tools, Inc. v. American Tool, Inc.*, 678 F.2d 1253, 1259 (5th Cir. 1982) (the grant of an exclusive dealership is not a *per se* violation of the Sherman Act because "such a grant does not seek to impose resale price maintenance on the distributor"). Any vertical non-price restriction may affect resale prices, yet the Supreme Court has held that such restrictions are nonetheless to be evaluated under the rule of reason. *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 57, 97 S. Ct. 2549, 2561, 53 L.Ed.2d 568, 584 (1977).

[4] The Supreme Court's recent decision in *Monsanto Co. v. Spray-Rite Service Corp.*, ____U.S.____, 104 S.Ct.

1464, ____L.Ed.2d____, *reh'g denied,* 104 S. Ct. 2378 (1984), further confirms that this circuit's divergence from the *Cernuto* rationale is correct. In *Monsanto,* the Court held that an antitrust plaintiff cannot survive a directed verdict motion merely by showing a manufacturer terminated a price-cutting distributor in response to or following complaints by other distributors. *Id.* at ____, 104 S. Ct. at 1468. The Court noted two important distinctions in distributor-termination cases. The first is the distinction between concerted and independent action—only the former is proscribed by the Sherman Act. *Id.* at ____, 104 S. Ct. at 1469. Thus, under *United States v. Colgate & Co.,* 250 U.S. 300, 307, 39 S. Ct. 465, 468, 63 L.Ed. 992 (1919), it is permissible for a manufacturer, acting independently, to terminate any distributor for its failure to comply with the manufacturer's suggested retail prices.

[5] The second distinction is between concerted action to set prices and concerted action on non-price restriction—the former is illegal *per se* while the latter is evaluated under the rule of reason. *Id.* at ____, 104 S. Ct. at 1469. The Court conceded that these distinctions are difficult to apply in practice because both the conduct of the parties and the economic effect of that conduct may be similar or identical in many cases. *Id.* at ____, 104 S. Ct. at 1470. However, in *Monsanto* the Court chose not to deal with the underlying theoretical difficulties of the *per se* rule[1] Instead, the Court sought to

1. The validity of distinction between vertical price restraints and non-price restraints has been the subject of scholarly discussion. *See e.g.,* Bork, Vertical Restraints: Schwinn Overruled, 1977 Sup. Ct. Rev. 171, 180-81 (1977); Posner, The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision, 45 U. Chi. L. Rev. 1, 7-8 (1977). Posner, The Next Step in the Anti-trust Treatment of Restricted Distribution: Per Se Legality, 48 U. Chi. L. Rev. 6, 9 (1981).

Sharp urges us to evaluate all vertical restraints under the rule of reason. This argument faces a long history of the application of the *per se* rule against vertical price restraints. *Dr. Miles Medical Co. v. John D. Park & Sons Co.,* 220 U.S. 373, 31 S. Ct. 376, 55 L.Ed. 502 (1911). Our resolution of this case makes it unnecessary for us to reach or rule on Sharp's contention.

ensure that legitimate conduct on the part of the manufacturers and distributors would not be penalized due to the ambiguity of the legal rule. It is perfectly legitimate, and expected, for distributors to complain about the price cutting of their rivals. It is also legitimate for a manufacturer to terminate a price cutter either independently or pursuant to a non-price agreement. The mere fact that a manufacturer terminates a price cutter folowing or in response to dealer complaints does not determine whether the manufacturer is acting independently, pursuant to a non-price agreement or pursuant to a price agreement. To allow evidence of termination following or in response to complaints to serve as the sole basis for the award of treble damages to the terminated dealer would tend to discourage legitimate dealer complaints and legitimate manufacturer action in the face of such complaints. By disrupting communications between manufacturer and dealer it would create "an irrational dislocation in the market." *Id.* at ____, 104 S. Ct. at 1470.

[6] It is possible to interpret *Monsanto* as saying merely that a manufacturer can terminate a price cutter, whether or not a complaining dealer "agrees," as long as the manufacturer is acting for some reason other than "just knuckling under to the [complaining dealer's] desire for less

competition." *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 744 (7th Cir. 1982). Such an interpretation could make *Monsanto* consistent with *Cernuto*. *Id.; see also Edward J. Sweeney & Sons, Inc. v. Texaco, Inc.*, 637 F.2d 105, 111 (3d Cir. 1980), *cert. denied*, 101 S. Ct. 1981 (1981). However, this interpretation would lead to the very "irrational dislocations" that *Monsanto* sought to avoid. The jury, under *Cernuto*, is required to determine whether the manufacturer's motivation was one of terminating "free riders" or one of reducing price competition, yet in either case the manufacturer's attitude will be one of hostility toward price cutters. As Judge Posner has put it, there is a "certain unreality" in trying to tell these motivations apart. *Valley Liquors, supra*, 678 F.2d at 744. Therefore, the manufacturer which desires to terminate a price cutter because of its free riding will be deterred from this legitimate action because it is indistinguishable, except perhaps to a mind reader, from what *Cernuto* prohibits, i.e., termination of a price cutter because of its price cutting.

The instant case well illustrates the problem. If, confronted with Hartwell's complaints, Sharp determined that BEC's price cutting was undermining Hartwell's incentive to promote Sharp calculators (or simply that it was preferable to terminate BEC because of its poor sales record), Sharp had a perfect right to terminate BEC. Sharp's legal counsel, however, would be unable to advise Sharp of a means of safely accomplishing termination if, as under *Cernuto*, Sharp's antitrust liability turned solely on a jury's guess as to Sharp's motivation. Thus, Sharp would be prevented from exercising its legal rights merely because its information originated in a dealer complaint,

the very "irrational dislocation" *Monsanto* sought to prevent.[2]

Monsanto did not expressly disapprove the *Cernuto* rule. Indeed, the Court cited, in support of its holding, cases such as *Sweeney, supra*, which follow *Cernuto*. However, the issue in *Monsanto* was the quantity of evidence necessary to infer a price fixing agreement, not whether it was necessary to show such an agreement at all. Nothing in *Monsanto* suggests that liability can be found without any evidence of a price fixing agreement. Rather, the language of *Monsanto* can only indicate the Court's belief that a price fixing agreement is a requirement for *per se* liability in distributor-termination cases. For example, the Court indicated that a plaintiff must show that the "distributors are not making independent pricing decisions." *Monsanto, supra*, ____U S. at ____, 104 S. Ct. at 1470. The Court also stated that "it is of considerable importance that independent action by the manufacturer, and concerted action on nonprice restrictions, be distinguished from price-fixing agreements, since under present law the latter are subject to per se treatment and treble damages." *Id.* Finally, the Court defined the concept of "common scheme" as including communication between the parties as to an agreement on price. *Id.* at ____, 104 S. Ct. at 1471 n.9.

[7] For these reasons we hold that, in order for a manufacturer's termination of a distributor to be illegal

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2. [D]ealer complaining is likely whenever there is discounting by free riders, because most dealers are harmed by such conduct. The manufacturers cannot prevent the complaining. Yet if it occurs the manufacturer may have to abandon even nonprice restrictions in distribution, because any action it takes against a discounter may be deemed to be tainted by price-fixing. Posner, The Next Step, *supra* note 1, at 13.

per se, it must be pursuant to a price maintenance agreement with another distributor. That distributor must expressly or impliedly agree to set its prices at some level, though not a specific one. The distributor cannot retain complete freedom to set whatever price it chooses. The jury instructions in this case failed to reflect this standard and therefore were critically defective.[3]

III

Sharp contends that the evidence is insufficient to raise a jury issue as to whether Sharp and Hartwell entered into a price maintenance agreement. Sharp therefore argues that we should reverse the district court's denial of its motions for directed verdict and for judgment notwithstanding the verdict and order BEC's complaint dismissed.

[8] When a party moves for a judgment as a matter of law, the court should consider the evidence "in the light and with all reasonable inferences most favorable to the party opposed to the motion." *Boeing Co. v. Shipman,* 411 F.2d 365, 374 (5th Cir. 1969). A court may only take a case from the jury if the evidence is such that reasonable men could arrive at only one verdict. *Id.* To grant the relief sought by Sharp, we should also test the proof in terms of a fact finder operating under the proper legal concepts articulated in Part II above.

[9] Applying this standard to the case at bar, we hold that the evidence was sufficient to support a properly

3. If, on retrial, the district court again chooses to use special interrogatories, it may wish to follow either the form of the first interrogatory in *Monsanto,* __U.S.__ n.2, 104 S. Ct. 1467, n.2 or the bifurcated form of the first and second interrogatories in *Pierce v. Ramsey Winch,* 753 F.2d at 422, 423 n.6.

instructed jury verdict in BEC's favor. While it is true that there was little, if any, direct evidence that Sharp and Hartwell reached an agreement as to price, we think the jury reasonably could infer such an agreement from the evidence as a whole.

There was evidence that, even before Hartwell became a dealer, Sharp sought BEC's adherence to the suggested retail price list. BEC produced evidence tending to show that it was not "free-riding" and that its sales performance was equal to Hartwell's. The logical inferences from such evidence, if drawn by the jury, could support a finding that BEC's termination was not due to the reasons Sharp suggests. *See Fragale & Sons Beverage Co. v. Dill,* 760 F.2d 469, 474 (3d Cir. 1985).

In addition, there was evidence that Hartwell usually followed Sharp's suggested prices. There was also evidence that Hartwell sought to encourage BEC to follow these prices. Finally, the record shows that Hartwell complained vigorously to Sharp about BEC's pricing and that ultimately Sharp responded by terminating BEC. This evidence, taken as a whole and viewed in the light most favorable to BEC, could support an inference that Sharp and Hartwell had agreed that Hartwell would follow Sharp's suggested retail prices and that BEC's termination was pursuant to this agreement.

For these reasons Sharp was not entitled to judgment as a matter of law.

IV

The critical error in the jury instructions alone requires reversal. Two further issues should be addressed because they are likely to arise on retrial. The first issue involves

an evidentiary ruling. At trial, Sharp sought to introduce certain documents to confirm its policy of terminating dealers who failed to meet sales quotas. Defendant's Exhibit 52 is a Sharp document sent to Sharp Vice-President H. Kawai, one of the men responsible for BEC's termination, in May 1972. The document indicates that BEC made only 45% of its sales quota. Defendant's Exhibit 53 is a Sharp document sent to sales representatives and managers, as well as Kawai, in May, 1972; it states that dealers who fall below 50% quota should be replaced.

[10] Sharp contends that the district court erroneously excluded these documents as hearsay. We agree. " 'Hearsay' is a statement, other than one made by the declarant while testifying at trial or hearing, offered in evidence to prove the truth of the matter asserted." Fed. R. Evid. 801 (c). Sharp was not offering these documents for the purpose of proving the truth of the statements contained therein. Defendant's Exhibit 52 was not offered to show that BEC had only made 45% of its quota but to show Sharp *believed* BEC had only made 45% of its quota. *See Moore v. Sears, Roebuck & Co.*, 683 F.2d 1321, 1322 (11th Cir. 1982) (corporate memoranda concerning employee's performance were admissible, not to show that employee actually performed poorly, but to show that corporation believed that employee's performance was poor). Defendant's Exhibit 53 was offered to show that Kawai, who *received* the document, believed that Sharp's policy was to terminate dealers who fell below 50% of quota, whether or not this was in fact Sharp's policy.

Exhibit 53 would also be admissible for the purpose of showing what Sharp's policy actually was because it did not directly declare that "termination is Sharp's policy"

but merely indicated that policy indirectly by saying that dealers falling below 50% of quota should be replaced. *See* McCormick, *Evidence* § 249. Even if hearsay, the document would fall within the "state of mind" exception. Fed. R. Evid. 803(3).

The district court's memorandum and order indicated that even if the excluded documents were admissible, they related to policies and states of mind "too far removed in time from the termination to be relevant." Although the district court has broad discretion in the admission of evidence, *Carlton v. Shelton*, 722 F.2d 203, 206 (5th Cir.), *cert. denied*, 104 S. Ct. 2389 (1984), that discretion was improperly exercised here. Much of the evidence BEC relies upon relates to Sharp's actions long before the termination. Indeed, the district court properly admitted Plaintiff's Exhibit 6, a Sharp document from February 1971, which reflected Sharp's policy at that time of enforcing minimum retail pricing on another product line. Exhibits 52 and 53 provide explanations for Sharp's actions other than a pure concern for BEC's pricing. Furthermore, the fact that Sharp believed in 1972 that BEC had only met 45% of its quota is relevant to its decision to terminate BEC, when faced with an ultimatum from a more successful dealer, one year later. It was error to exclude Defendant's Exhibits 52 and 53.

[11] Defendant's Exhibits 54 and 55 are Sharp documents that were received by Thomas Burkholder, Sharp's Texas representative, in May and September, 1972. They set Burkholder's sales quota and indicate the importance of meeting that quota. Exhibits 54 and 55 were also improperly excluded as hearsay. They were offered to show their effect on Burkholder, *i.e.*, to show that he was under pressure to meet sales quotas. The district court

correctly ruled that Defendant's Exhibits 54 and 55, which did not relate to dealer performance or quotas, were not sufficiently relevant to be admissible.

V

The second issue involves Sharp's contention that the district court accepted an erroneous method of computing damages. First, Sharp claims that Hartwell's sales should not have been used as a yardstick to measure BEC's damages. Second Sharp argues that the plaintiff's damage expert improperly used BEC's gross profit margin, instead of Hartwell's lower gross profit margin, to calculate damages.

[12] An antitrust plaintiff is not required to "prove with exact particularity what its success might have been in the market in the absence of illegal conduct of another." *Multiflex, Inc. v. Samuel Moore & Co.*, 709 F.2d 980. 995 (5th Cir. 1983), *cert. denied,* 104 S. Ct. 1594 (1984). The use of Hartwell as a yardstick was reasonable because he sold the same product in the same area. He sold to similar customers. While both were in business, their sales volume was roughly equivalent. Furthermore, there was evidence that BEC's expenses were lower than those of Hartwell. Although Sharp pointed to possible defects in the method used by BEC, consideration of such defects was properly left to the jury since the method chosen was not a matter of pure speculation. *Pierce v. Ramsey Winch, supra,* 753 F.2d at 440. We conclude that the district court did not err in accepting BEC's method of calculation damages.

VI

The district court correctly ruled that Sharp was not entitled to a judgment as a matter of law. We reverse the

judgment appealed from because the case was submitted to the jury on an erroneous theory of liability. We remand for further proceedings not inconsistent with this opinion. REVERSED AND REMANDED.

JONES, Circuit Judge, concurring:

I concur in the judgment requiring remand for retrial because this court is bound by the decision in *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 104 S. Ct. 1464, 79 L.Ed.2d 775 (1984). However, I believe this case perfectly illustrates the arguments why vertical price restraints should be tested under antitrust's Rule of Reason[1] rather than, as *Monsanto* continues to require, per se illegality. There is no social benefit to subjecting manufacturers' pricing relationships with their distributors to potential per se illegality where they operate in markets whose interbrand competitiveness overwhelms any detrimental effects of those relationships. And, although *Monsanto* moves toward alleviating the threat of unwarranted treble-damage action, the abiding uncertainty suggests that the Supreme Court would more wisely jettison the precedent that led to the rule of per se illegality for vertical price restraints.

The flaws in *Monsanto's* continued recognition of per se illegality are highlighted by this case. First, it is difficult to conceive how, in the real world, the subjection of vertical price restraints to per se illegality improves the functioning of the economy or enhances consumer welfare. Only atavistic devotees of the abacus or slide rule could fail to recall the remarkable history of the electronic

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1. *See Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 97 S. Ct. 2549, 53 L.Ed.2d 568 (1977).

calculator market during the last fifteen years. The range of available models, variety of functions that can be performed, and myriad optional enhancements have multiplied rapidly while the average prices have plummeted. The number of competing manufacturers has increased. To maintain their market position and profitability, manufacturers like Sharp have obviously been required to react quickly and imaginatively to changes in the marketplace. The record in this case reveals that both Sharp's market share and the retail prices of its calculators were declining in this period.[2] Nevertheless, as the result of the current state of antitrust law, Sharp is potentially held accountable in treble damages for terminating a distributor who, in Sharp's perception, failed to market its product adequately. To hold, as this court must, that Sharp cannot respond to changing market conditions with all of the competitive arrows in its quiver including, if necessary, a program to respond to "free riders" like BEC,[3] is to put Sharp at a potential competitive disadvantage. To limit Sharp's marketing options for its calculators may also limit the range of products available to the consumer of calculators. See Easterbrook, *Vertical Arrangements and the Rule of Reason,* 53 Antitrust L.J. 135 (1984). To isolate one factor in the relationship of Sharp and its distributors, i.e. whether Sharp required them to adhere to its published retail price lists, in this

2. Sharp faced 100 competitors. The prices of its calculators ranged from $500-1,000 in 1972 to $150-300 ten years later.

3. "Free riders" are distributors who market products by cutting their prices, to the neglect of customer and market-development services, which are performed by the distributor who has kept margins higher by not discounting. Frequently, the "free rider's" sales benefit from the services performed by the full-price dealer. *See* Posner, *The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision,* 45 U. Chi. L. Rev. 1, 6-10 (1977).

hectically competitive market is to ignore the fact that here have been no anticompetitive effects of the conduct in issue: prices declined and the number and quality of competing products increased. The larger conclusion that can be drawn from the scenario of this case is that assuming the continued variety, vitality and innovation of the American free enterprise system, it is unrealistic to conclude that measures taken by a manufacturer to enhance his product's marketability, whether related to price or not, are anticompetitive unless they are part of a program to enforce a manufacturer- or dealer-level cartel. *See* Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality,* 48 U. Chi. L. Rev. 6, 25 (1981).

As the majority opinion elegantly demonstrates, *Monsanto* has raised the level of proof required to submit a vertical price restraint case to the jury. However, its second flaw is that, despite so doing, it leaves a cloud of uncertainty and incongruity. The *Monsanto* standard, a "something more" formulation of a vertical price agreement,[4] provides little guidance for lower courts and counsel. Already, the Eighth Circuit has affirmed a finding of per se liability based upon a "price-related" conspiracy, which is totally at odds with today's interpretation on *Monsanto* by this Circuit. *See Victorian House Inc. v. Fisher Camuto Corp.,* 769 F.2d 466, 469 (8th Cir. 1985); *compare Bender v. Southland Corp.,* 749 F.2d 1205 (6th Cir. 1984). Most clever attorneys, like plaintiff's counsel in this case, will be able to generate sufficient evidence, even pursuant to the *Monsanto* stand-

4. 104 S. Ct. at 1471 n.9 ("evidence must be presented both that the distributor communicated its acquiescence or agreement, and that this was sought by the manufacturer").

ard, to withstand summary judgment review, and thus to exert substantial influence toward settlement of cases where no anticompetitive harm, or harm to the consuming public, really occurred. Moreover, the distinction between vertical price and non-price restraints can be difficult to draw, and because *Monsanto* retains a powerful incentive to describe a dealer's anti-trust complaints as being price-related, in order to secure the litigational benefit of the per se standard, such distinctions can be expected to be even more finely (and uselessly) articulated. *See generally* Hay, *Vertical Restraints after Monsanto,* 70 Cornell L.Rev. 418, at 431-435 (1985). Retention of the per se test of illegality for vertical price-maintenance will thus continue to inhibit the functioning of non-price restraints which the Supreme Court sees as generally beneficial. *Continental T.V., Inc. v. GTE Sylvania Inc.,* 433 U.S. 36, 97 S. Ct. 2549, 53 L.Ed.2d 568 (1977). In sum, the antitrust law of vertical restraints remains much in turmoil, to the detriment of potential defendants and the public, which suffers due to the limitation of distributional variety, but to the benefit of the legal class.

Semantic nuances are costly to businessmen in the real world. The Supreme Court has noted that, "per se rules of illegality are appropriate only when they relate to conduct that is manifestly anticompetitive. . . . 'there are certain agreements and practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use.' " *Northern Pacific R. Co. v. United States,* 356 U.S. 1, 5, 78 S. Ct. 514, 518, 2 L.Ed.2d

545 (1958) (quoted in *Continental T.V., Inc. v. GTE Sylvania Inc., supra,* 433 U.S. at 50, 97 S. Ct. at 2557.[5] Present economic understandings does not compel per se treatment of vertical price restrictions. On the contrary, Judge Easterbrook's analysis of *Monsanto* would appear to be correct:

> If restricted dealing and price arrangement are ordinarily procompetitive, if there is no real difference between the effects of price and non-price restraints, and if the objection to [vertical price restraints] is the same as that to other vertical restraints, then it follows that per se condemnation of [vertical price restraints] is anomalous.

Easterbrook, supra at 171. The Supreme Court should take the earliest opportunity to review its Russian roulette approach to vertical price restraints.

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5. For a discussion of the quirky and questionable legal history of the per se rule in vertical price restraint cases, see Brief of the United States as Amicus Curiae to the Supreme Court in the *Monsanto* case; see also Easterbrook, *supra*.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

Civil Action No. H-78-1020

BUSINESS ELECTRONICS CORPORATION, ET AL.,
Plaintiff

v.

SHARP ELECTRONICS CORPORATION, ET AL.,
Defendants.

MEMORANDUM AND ORDER

Presently pending before the Court is Defendant Sharp Electronic Corporation's (Sharp) Motion for Judgment Notwithstanding the Verdict, or, in the Alternative, For a New Trial. Rules 50(b) and 59, Fed. R. Civ. P. The Court, having considered carefully the motion, together with the briefs submitted by the parties, the evidence adduced at trial and the relevant law, concludes that the motion must be denied.

This action was originally filed in the Western District of Texas on July 11, 1975, alleging violations of the Sherman and Clayton Anti-Trust Acts, 15 U.S.C. §§ 1-31. The case was subsequently transferred to this district on June 7, 1978. A jury trial was commenced on October 17, 1983, and special verdicts were returned on November 4, 1983. Final judgment was entered on the jury verdicts on December 7, 1983; this motion for post-judgment relief was timely filed on December 19, 1983.

JUDGMENT N.O.V.

The standard governing a decision to grant or deny a motion for judgment notwithstanding the verdict (judgment n.o.v.) is that set forth in *Boeing v. Shipman,* 411 F.2d 365 (5th Cir. 1969) (en banc):

> On motions for directed verdict and for judgment notwithstanding the verdict the Court should consider all of the evidence—not just that evidence which supports the non-mover's case—but in the light and with all reasonable inferences most favorable to the party opposed to the motion. If the facts and inferences point so strongly and overwhelmingly in favor of one party that the Court believes that reasonable men could not arrive at a contrary verdict, granting of the motions is proper. On the other hand, if there is substantial evidence opposed to the motions, that is, evidence of such quality and weight that reasonable and fair-minded men in the exercise of impartial judgment might reach different conclusions, the motions should be denied, and the case submitted to the jury. A mere scintilla of evidence is insufficient to present a question for the jury. The motions for directed verdict and judgment n.o.v. should not be decided by which side has the better of the case, nor should they be granted only where there is a complete absence of probative facts to support a jury verdict. There must be a conflict in substantial evidence to create a jury question. However, it is the function of the jury as the traditional finder of facts, and not the Court, to weigh conflicting evidence and inferences, and determine the credibility of witnesses.

Id. at 374-75 (footnote omitted). *See also Affiliated Capital Corp. v. City of Houston,* 735 F.2d 1555, 1563

(1984); *Languirand v. Hayden,* 717 F.2d 220, 228 (5th Cir. 1983); *Aero Inten. v. United States Fire Ins. Co.,* 713 F.2d 1106, 1109-10 (5th Cir. 1983).

In the motion for judgment n.o.v., Sharp argues that (1) there was insufficient evidence to prove that Sharp and Codefendant Hartwell entered into a retail price maintenance agreement or that Business Electronics Corp. (BEC) was terminated in furtherance of the alleged agreement and (2) termination of a dealer in order to eliminate intrabrand price competition for a competing dealer is a "rule of reason" rather than a *per se* offense under § 1 of the Sherman Act.

Initially, the Court must address the second of these contentions: that termination of a distributor in furtherance of an agreement to eliminate intrabrand price competition should be judged under the rule of reason standard, rather than that of the harsh *per se* one. Sharp analogizes such termination to the decision to grant to one distributor an exclusive territorial dealership, a decision —which Sharp correctly points out—judged under the rule of reason standard.

On December 5, 1983, the Supreme Court heard oral argument in the case of *Monsanto Co. v. Spray-Rite Service Corp.,* No. 82-914. Numerous *amici,* including the Solicitor General, argued that the economic effect of such a "contract, combination . . . or conspiracy" differs little from that which arises from agreements on non-price restrictions, and should therefore be judged by the same standard. *See generally* Posner, *The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision,* 45 Chi.L.Rev. 1 (1977). The Court however, noting that neither party had raised this issue at trial or

at the appellate court, declined to reach the question. *Monsanto Co. v. Spray-Rite Service Corp.,* ____U.S.____, 104 S. Ct. 1464, 1469 & n.7 (1984).

In contrast to *Monsanto* however, Sharp repeatedly urged the Court, both before and during trial, that the standard applicable to dealer-termination cases such as this is the rule of reason. The Court rejected this position and instructed the jury on the *per se* standard. While it is true that *Monsanto* does not prohibit application of the rule of reason standard, neither does it mandate it. Moreover, the Court finds Justice Brennan's concurring opinion persuasive on this point. The *per se* interpretation has been extant for 73 years, and Congress in that time has not seen fit to disturb that interpretation. *Monsanto,* 104 S. Ct. at 1473 (Brennan, J., concurring). Without a clear mandate to the contrary, this Court likewise declines. Accordingly, there was no error in the application of the *per se* standard to Sharp's conduct. *Cf. Northern Pac. R. Co. v. United States,* 356 U.S. 1, 5 (1958).

In *Monsanto,* the Court addressed the standard of proof governing sufficiency of evidence in a dealer-termination case where termination was allegedly in response to intraband price-cutting. Section 1 of the Sherman Act specifically requires a conspiracy or combination between a manufacturer and its distributors to reach conduct proscribed by the Act. Unilateral action by the manufacturer is not sufficient. Moreover, to be judged under the *per se* standard, such combination or conspiracy must constitute concerted action to set prices, and not merely concerted action on other non-price restrictions. The Court noted homever, that an attempt to differentiate between these two extremes solely by assessing the "market impact" of the complained of conduct, *Continental T.V., Inc. v. GTE*

Sylvania Inc., 433 U.S. 36, 51 (1977), was in practice extremely difficult. In many cases, "the economic effect . . . of the conduct described . . . [would be] similar or identical." *Monsanto,* 104 S. Ct. at 1470. The danger of the "market impact" approach, recognized by the Court, was that the jury might infer the existence of a concerted price-fixing agreement from "highly ambiguous evidence", thus subjecting the defendant to the *per se* standard and its concomitant treble damages.

Accordingly, in order to carry the burden of proving the existence of a price-setting agreement, plaintiff must show something more than the existence of price-cutting complaints by co-distributors, or even that plaintiff's termination followed such complaints. *Id.* The plaintiff must produce "evidence that tends to exclude the possibility that the manufacturer and non-terminated distributor were acting independently." *Id.* at 1471.

In the instant case, that distributor complaints were made and that BEC's termination followed is not seriously contested. Sharp does vigorously maintain that there is insufficient evidence to link these two events into a conspiracy. The Court does not agree. Sharp published and disseminated a retail price list to its dealers. This price list was closely followed by "letters" from Sharp to its dealers. When BEC failed to adhere to these suggested retail prices, Defendant Hartwell complained vocifierously to Sharp. Hartwell's outcry eventually escalated beyond mere complaints to an "either-or" ultimatum. Sharp terminated BEC immediately thereafter. Applying the *Boeing* and *Monsanto* standards to these and the totality of the facts of the case, the Court finds there was sufficient evidence for the jury to have concluded that Sharp and Hartwell were parties to an agreement to set product

retail prices and, in furtherance of that agreement, that BEC was terminated for refusing to adhere to those prices. *Monsanto,* 104 S. Ct. at 1471 & n.10.

In its motion for judgment n.o.v., Sharp also contends that there was insufficient evidence to support the jury damage award. While it is true that BEC must carry the burden of demonstrating a "rational quantum of actual damages" stemming from the anti-trust violations, that burden is somewhat lighter than that required to prove the initial fact of damages. This Circuit has consistently held that the plaintiff will not be required to "prove with exact particularity what its success might have been in the market in the absence of illegal conduct of another." *Multiflex, Inc. v. Samuel Moore & Co.,* 709 F.2d 980, 995 (5th Cir. 1983) (citing cases), *cert. denied,* ____ U.S.____, 104 S. Ct. 1594 (1984).

The Court notes that the arguments advanced here are essentially those which Sharp presented to the jury during trial. Both sides then availed themselves of expert testimony on these points. The economic model presented by Plaintiff's expert, Mr. Chernow, was ably attacked at that time. The jury was entitled to weigh and evaluate the opposing testimony, and the Court will not now invade the traditional province of the fact finder by substituting its judgment. It is not the function of the Court "to weigh the conflicting evidence and inferences, and determine credibility of witnesses." *Boeing,* 411 U.S. at 375.

Finally, Sharp contends that Mr. Chernow's economic model included a projection of lost interest income, and characterizes that projection as an improper attempt to obtain prejudgment interest. *Heatransfer Corp. v. Volkswagenwerk, A.G.,* 553 F.2d 964, 986 & n.20 (5th Cir.

1977), *cert. denied,* 434 U.S. 1087 (1978). The model characterizes this element of damages, however, as lost interest income which is normally recoverable in this circuit. Since the model made no attempt to base this recovery on the statutory claim condemned in *Volkswagenwerk,* the Court finds no error in the model. *Multiflex,* 709 F.2d at 996-97.

NEW TRIAL

The decision to grant or deny a motion for a new trial is one committed to the sound discretion of the Court. *Reeves v. General Foods Corp.,* 682 F.2d 515 (5th Cir. 1982); *Martinez v. Food City, Inc.,* 658 F.2d 369 (5th Cir. 1981). The standard here is lower than that applicable under a motion for judgment n.o.v. or a directed verdict. The trial judge may set aside the verdict and grant a new trial if, in his opinion, the verdict is either against the great weight of the evidence or will result in a miscarriage of justice, even though there may be substantial evidence in support. *Shows v. Jamison Bedding,* Inc., 671 F.2d 927 (5th Cir. 1982). Moreover, the court is not required to view all the evidence in a light most favorable to the non-movant, but may weigh and evaluate the evidence in much the same fashion as the jury. This Court will not order a new trial, however, merely because it may have reached a different verdict. The verdict must be contrary to the *great* weight of the evidence. *Cf. United States v. Bucon Const. Co.,* 430 F.2d 420 (5th Cir. 1970). *See generally* 11 C. Wright & A. Miller, *Federal Practice & Procedure: Civil* § 2806 (1973).

The trial of this antitrust action was both lengthy and exceedingly complex. The issues presented, and their evidentiary support, were ably contested by the attorneys

for BEC and Sharp. In its brief in support of the motion for a new trial, Sharp has provided the Court with a detailed argument of the evidence adduced at trial. Nonetheless, the Court has conducted its own exhaustive review of the 13 volume transcript of the proceedings. And while that review has revealed conflicting evidence on virtually every point, the Court is unable to conclude that the jury's verdict is against the great weight of the evidence.

Court's Instructions to the Jury

When reviewing alleged error in the jury instructions, the district court will not grant a new trial or otherwise disturb the jury's verdict "unless refusal to take such action appears to the court inconsistent with substantial justice." Rule 61, Fed. R. Civ. P. Moreover, challenged jury instructions will not be considered in isolation from the remainder of the charge. Rather, the court will look to the charge as an "integrated whole", together with the allegations presented in the complaint, the evidence adduced at trial and arguments of counsel. *Bunch v. Walter,* 673 F.2d 127, 131 (5th Cir. 1982); *Coughlin v. Capitol Cement Co.,* 571 F.2d 290, 300 (5th Cir. 1978) (citing cases). "If, viewed in that light, [they] are comprehensive, balanced, fundamentally accurate and not likely to confuse or mislead the jury, the charge will be deemed adequate." *Bunch, supra* at 132, *quoting, Scheib v. Williams-McWilliams Co.,* 628 F.2d 509, 511 (5th Cir. 1980).

In the brief accompanying the Rule 59 motion, Sharp advances detailed arguments which allege error in the inclusion or exclusion of 13 separate instructions. These arguments are, however, identical to those rejected by

the Court both in conference and on the record outside the presence of the jury. Sharp's Point of Error Nos. 11-15, 17, 21 & 22 in the main seek repetitive instructions which were covered elsewhere in the charge. Point of Error Nos. 16 & 19 deal with the "rule of reason" standard and the "complaints followed by termination" issue. Both of these contentions have been adequately discussed and denied earlier in this Memorandum. In Point of Error No. 18, Sharp attacks the circumstantial evidence instruction given by the Court. This instruction, however, is identical to that found in Devitt & Blackmar, *Federal Jury Practice and Instructions,* §§ 15.02 & 72.02 (1977), and approved by the Fifth Circuit in *United States v. Clark,* 506 F.2d 416 (5th Cir.), *cert. denied,* 421 U.S. 967 (1975). In Point of Error No. 20, Sharp alleges that use of the word "understanding" "improperly allowed and encouraged the jury to find an antitrust violation based on something less than an agreement." The Court finds that, reading the charge as a whole but specifically in regard to that section dealing with Special Interrogatory No. 1, inclusion of the word "understanding" was in no way misleading or confusing. Finally, in Point of Error No. 23, Sharp alleges that the Court mischaracterized Sharp's defense to this action. Sharp's attorneys ably argued their client's case to the jury, including all possible defenses. Reading the challenged instruction as part of the "integrated whole", the Court concludes that if such a charge was erroneous, it was clearly harmless.

Admissability of Evidence

Also in the Rule 59 motion, Sharp challenges the Court's admission of the "Gold Memorandum" and the

exclusion of several of Sharp's exhibits and the testimony of two defense witnesses associated with the excluded exhibits. The Fifth Circuit has repeatedly emphasized that "the trial court generally has broad discretion in the admission of evidence." *Carlton v. Shelton,* 722 F.2d 203, 206 (5th Cir. 1984); *Ramos v. Liberty Mutual Ins. Co.,* 615 F.2d 334, 340 (5th Cir. 1980). After a careful review of the record, the Court finds no error in the admission of the Gold Memorandum or the exclusion of Sharp's exhibits or testimony.

Sharp first challenges the authenticity of the Gold Memorandum. Determination by the court of the authenticity of an exhibit is committed to the sound discretion of the court, *United States v. Gorel,* 622 F.2d 100 (5th Cir. 1979), *cert. denied,* 445 U.S. 943 (1980), and requires only a prima facie showing. As is the case here, a document's "physical appearance, . . . contents, and letterhead may in combination authenticate the writing." 5 Weinstein & Berger, *Weinstein's Evidence,* ¶ 901(b)(4) [02] at 901-51 (1983); Rule 901 (b)(4), Fed. R. Evid. Sharp's contention that the memorandum is not relevant with sufficiency. Evidence is relevant if it has "any tendency to make the existence of any fact . . . more probable or less probable than it would be without the evidence." Rule 401, Fed. R. Evid.

Sharp further challenges the exclusion of Defendant's Exhibits Nos. 52-55, 81, 81a, 82 & 82a. Exhibits 52-55 were excluded by the Court as hearsay. Sharp alleges that even if the exhibits were hearsay, they fall under the "state of mind" exception to the general rule. Rule 803 (3), Fed. R. Evid. Sharp also alleges that the excluded testimony of defense witness Burkholder is within the same exception. The Court again rejects this position.

Evidence presented outside the presence of the jury revealed the disputed exhibits and testimony relate to policies and/or subjective states of mind too far removed in time from the termination to be relevant to the facts of this case. Sharp's Exhibit Nos. 81, 81a, 82 & 82a and the associated testimony of defense witness Wiles all relate to the alleged appreciation of rental property purchased by Plaintiff Ehrensberger after termination. Sharp contends that such evidence is relevant to the issue of mitigation of damages. The Court concludes that, given the speculative nature of this evidence, its exclusion, if erroneous, was clearly harmless.

Finally, Sharp contends that the attorney for BEC engaged in improper argument to the jury in regard to use of deposition testimony. The Court concludes that Plaintiff's attorney was not attempting to denigrate the deposition testimony of Mr. Kawai. Regardless, even if such argument was improper, it was cured by the Court's instruction to the jury dealing with the use of deposition testimony.

For the reasons stated above, the Court hereby ORDERS:

Defendant's Motion for Judgment Notwithstanding the Verdict, or, in the Alternative, For a New Trial, is in all respects DENIED.

This is a FINAL JUDGMENT.

The Clerk shall file this Memorandum and Order and provide counsel for all parties with a true copy.

DONE at Houston, Texas this 28th day of September 1984.

/s/ WOODROW SEALS
United States District Judge

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 84-2618

D.C. Docket No. CA-H-78-1020

BUSINESS ELECTRONICS CORP.,
Plaintiff-Appellee,

versus

SHARP ELECTRONICS CORP.,
Defendant-Appellant.

Appeal from the United States District Court for the Southern District of Texas

Before CLARK, Chief Judge, THORNBERRY, and JONES, Circuit Judges.

JUDGMENT

This cause came on to be heard on the record on appeal and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the District Court in this cause is reversed, and the cause is remanded to the District Court for further proceedings in accordance with the opinion of this Court.

IT IS FURTHER ORDERED that plaintiff-appellee pay to defendant-appellant the costs on appeal, to be taxed by the Clerk of this Court.

January 21, 1986

JONES, Circuit Judge, concurring.

ISSUED AS MANDATE:

APPENDIX D

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 84-2618

BUSINESS ELECTRONICS CORP.,
and KELTON EHRENSBERGER, ETC.,
Plaintiffs-Appellees,

versus

SHARP ELECTRONICS CORPORATION,
Defendant-Appellant.

Appeal from the United States District Court for the
Southern District of Texas

ON SUGGESTION FOR REHEARING EN BANC
(Opinion 1/21/86, 5 Cir., 198_, ____F.2d____)

(February 24, 1986)

(Filed February 20, 1986)

Before CLARK, Chief Judge, THORNBERRY and JONES, Circuit Judges.

PER CURIAM:

(√) Treating the suggestion for rehearing en banc as a petition for panel rehearing, it is ordered that the petition for panel rehearing is DENIED. No member of the panel

nor Judge in regular active service of this Court having requested that the Court be polled on rehearing en banc (Federal Rules of Appellate Procedure and Local Rule 35), the suggestion for Rehearing En Banc is DENIED.

( ) Treating the suggestion for rehearing en banc as a petition for panel rehearing, the petition for panel rehearing is DENIED. The judges in regular active service of this Court having been polled at the request of one of said judges and a majority of said judges not having voted in favor of it (Federal Rules of Appellate Procedure and Local Rule 35), the suggestion for Rehearing En Banc is DENIED.

ENTERED FOR THE COURT:

/s/ Charles Clark
CHIEF JUDGE

Supreme Court, U.S.
FILED
JUN 19 1986
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

October Term, 1985

NO. 85-1910

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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IN THE

Supreme Court of the United States

October Term, 1985

NO. 85-1910

BUSINESS ELECTRONICS CORPORATION,
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v.

SHARP ELECTRONICS CORPORATION,
Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

ARGUMENT

Business Electronics Corporation ("BEC") asserts in its Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit ("Petition") that Supreme Court review is warranted because the United States Court of Appeals for the Fifth Circuit decided an important question of federal law which has not been, but should be, resolved by this Court.

The question submitted for review as phrased by BEC is not the one determined by the Court of Appeals. The question in fact resolved by the Court of Appeals was whether an agreement between a manufacturer and a dealer to terminate another dealer because of the latter's discount pricing constitutes a vertical price fixing agreement *per se* illegal under § 1 of the Sherman Act, 15 U.S.C. § 1, where

there is no claim of any agreement between the manufacturer and the remaining dealer to raise, maintain or otherwise fix resale prices. *Business Electronics Corp. v. Sharp Electronics Corp.*, 780 F.2d 1212, 1215-16 (5th Cir. 1986); *see* Appendix to Petition at pp. 6a-8a. The Court of Appeals correctly held that under *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), the answer is no.

Respondent, Sharp Electronics Corporation,[1] respectfully submits that if any question presented by the Court of Appeals' decision is deemed appropriate for review by this Court, it cannot be reviewed without determining the larger, and dispositive, question of whether vertical price fixing agreements, however defined, should continue to be deemed *per se* illegal under § 1. Respondent has filed a Cross-Petition for Writ of Certiorari ("Cross-Petition") (No.) in which it has asked the Court to review this larger question, and, ultimately, to rule that all vertical restraints, including vertical price restraints, should be evaluated under the rule of reason. Such a decision by this Court would moot any issue raised by BEC's Petition herein.

[1] Pursuant to Rule 28.1 of the Supreme Court Rules, Sharp Electronics Corporation represents that its parent corporation is Sharp Corporation and that it has no subsidiaries or affiliates.

CONCLUSION

For the foregoing reasons, respondent respectfully requests that the Petition not be granted, unless this Court also determines to grant the Cross-Petition.

Dated: June 19, 1986

Respectfully submitted,

s/ PETER J. GARTLAND

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CERTIFICATE OF SERVICE

This is to certify that on the 19th day of June, 1986, three true and correct copies of the foregoing Brief in Opposition to Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit were served by mail on counsel of record for petitioner, Stephen D. Susman, Susman, Godfrey & McGowan, 2400 Allied Bank Plaza, Houston, Texas 77002.

s/ PETER J. GARTLAND

PETER J. GARTLAND

Supreme Court, U.S.
FILED
MAY 18 1987
JOSEPH F. SPANIOL, JR.
CLERK

Nos. 85-1910 and 85-2094

In the Supreme Court of the United States

OCTOBER TERM, 1986

BUSINESS ELECTRONICS CORPORATION, PETITIONER

v.

SHARP ELECTRONICS CORPORATION

SHARP ELECTRONICS CORPORATION, CROSS-PETITIONER

v.

BUSINESS ELECTRONICS CORPORATION

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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SUPPLEMENTAL BRIEF FOR RESPONDENT/ CROSS-PETITIONER PURSUANT TO RULE 22.6

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In the Supreme Court of the United States

OCTOBER TERM, 1986

Nos. 85-1910 and 85-2094

BUSINESS ELECTRONICS CORPORATION, PETITIONER

v.

SHARP ELECTRONICS CORPORATION

SHARP ELECTRONICS CORPORATION, CROSS-PETITIONER

v.

BUSINESS ELECTRONICS CORPORATION

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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SUPPLEMENTAL BRIEF FOR RESPONDENT/ CROSS-PETITIONER PURSUANT TO RULE 22.6

On May 13, 1987, the United States filed a brief *amicus curiae* in which it (a) recommended that the Court deny the petition, despite a conflict in the circuits on the question of how to define vertical price fixing in the dealer termination context, because of the "strong trend toward adoption of the rule espoused by the court below" (U.S. Br. 12); and (b) expressed no views on whether the Court should grant the cross-petition, which raises the question

of whether vertical price restraints should be subject to the rule of reason, because the statute appropriating funds for the operation of the Department of Justice prohibits the Solicitor General from undertaking any activity to alter the *per se* prohibition on resale price maintenance. U.S. Br. 15.

Respondent/Cross-Petitioner Sharp Electronics Corporation ("Sharp") respectfully submits that certiorari should be granted notwithstanding the government's peculiar submission.

1. With respect to the petition, the essence of the government's position is that the appropriate definition of vertical price fixing was resolved by *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984). The government maintains that under *Monsanto*, an agreement on prices is a necessary element of a vertical price fixing case, that the Fifth Circuit's decision shows that the courts of appeals understand this rule and will follow it in the future, and that any need for granting the petition is therefore obviated. U.S. Br. 12. Contrary to the government's assertions, however, the question raised by the petition was the subject of a split among the circuits prior to *Monsanto*, remains the subject of a conflict, and (for both legal and practical reasons) urgently requires resolution by this Court.

While Sharp agrees that *Monsanto* requires proof of an actual price fixing agreement before *per se* liability attaches, the decision below does not reflect an application of *Monsanto* as such. Rather, the Fifth Circuit made plain that its decision was the product of pre-*Monsanto* precedent from within the Fifth Circuit. See Pet. App. 7a-9a. While the court of appeals read *Monsanto* as being consistent with the prior rule in the Fifth Circuit (*id.* at 9a-10a), it expressly acknowledged that it would be perfectly proper to read *Monsanto* the other way, *i.e.*, as consistent with decisions such as *Cernuto, Inc.* v. *United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979). Pet. App. 11a-12a.

Therefore, as new dealer termination cases arise outside the Fifth Circuit, the decision below can be cited for the proposition that *whatever* rule existed in the circuit prior to *Monsanto*, that rule should continue to be followed. Since most circuits that had considered the matter pre-*Monsanto* followed the *Cernuto* rule, see Pet. App. 8a, the decision below can be cited in support of adhering to that rule post-*Monsanto*. Thus, in *O.S.C. Corp. v. Apple Computer, Inc.*, 792 F.2d 1464 (9th Cir. 1986), the Ninth Circuit relied on its pre-*Monsanto* decision in *Zidell Explorations, Inc.* v. *Conval International, Ltd.*, 719 F.2d 1465 (9th Cir. 1983)—a case that expressly adopted the *Cernuto* standard—as setting forth the law in that Circuit on what constitutes vertical price fixing. 792 F.2d at 1467.

The government's contentions that there no longer is a split among the circuits and that the rule adopted by the Fifth Circuit has met with unanimous approval are demonstrably erroneous. Subsequent to *Monsanto*, the rule announced below was squarely rejected in *Victorian House Inc.* v. *Fisher Camuto Corp.*, 769 F.2d 466 (8th Cir. 1985), which held:

> A conspiracy between a wholesaler and one or more of its retailers to terminate a competing retailer on the basis of price constitutes a *per se* violation of the Sherman Act. *Cernuto Corp.* v. *United Cabinet Corp.*, 595 F.2d 164, 170 (3d Cir. 1979).

769 F.2d at 469. The government suggests that the *Victorian House* decision can largely be ignored. U.S. Br. 12. But companies such as Sharp, which may be named as defendants in antitrust actions in locations such as Minneapolis or St. Louis, cannot be so sanguine (or foolhardy).

Moreover, the government fails to point out that the Fifth Circuit's decision in this case has also been severely criticized by commentators:

> The Fifth Circuit's decision in *Business Electronics Corp.* badly distorted the *Monsanto* analysis. The *Monsanto* Court nowhere required that a plaintiff prove the existence of a *contract* between the supplier and the complaining dealer to maintain prices "at some level" resulting in the price-cutting dealer's termination before allowing a jury to find illegal price fixing.

Flynn, *The "Is" And "Ought" of Vertical Restraints After Monsanto Co. v. Spray-Rite Service Corp.*, 71 Corn. L. Rev. 1095, 1114 (1986) (emphasis in original).

Indeed, the government's suggestion that there is unanimity of any kind in this area will come as a surprise to the antitrust bar. To the contrary, if a supplier such as Sharp were to terminate a free riding dealer such as BEC in response to an "it's him or me" ultimatum from another dealer, the outcome of any resulting antitrust action would depend entirely upon the venue of the suit. In the Eighth Circuit the supplier would have engaged in a *per se* illegal price fixing agreement (*Victorian House*), in the Fifth Circuit there would be a jury question whether there was a *per se* illegal price fixing agreement (*Business Electronics Corp.*), and in the Fourth Circuit the supplier would prevail on summary judgment because a response to an "it's him or me" ultimatum is not deemed an agreement at all. See *Garment District, Inc.* v. *Bulk Stores Services, Inc.*, 799 F.2d 905, 909, 911 (4th Cir. 1986). This hardly reflects unanimity.

The third fundamental fallacy in the government's position is that its optimistic prediction as to the future trend of the law is of little real world utility. Sharp has dealers in every circuit. If Sharp wants to terminate its dealer in Pittsburgh and that dealer happens to be a discounter, Sharp finds itself in a quandary. Pittsburgh is in the Third Circuit, the Third Circuit decided *Cernuto*, and *Cernuto* makes any termination of a discounter an invitation to a lengthy and expensive antitrust suit. Sharp's problem is no less pronounced if the dealer in question is in Boston. The First Circuit has not yet spoken on the issue of what constitutes vertical price fixing. The only guidance counsel could offer would be the assurance that, in the sincere belief of the Solicitor General, the conflict "has largely abated," several circuits "appear to have" abandoned their prior positions, and the First Circuit "may well conclude" that the decision below, rather than the *Cernuto* rule, should be followed. U.S. Br. 12, 13. In making this observation, counsel would have to add that the First Circuit also "may well conclude" exactly the opposite, and that if the First Circuit follows *Cernuto* and the several other circuits that agree with *Cernuto*, Sharp can expect to write a check for treble damages.[1]

In sum, with the present confused state of the law, Sharp and every other national supplier must play Russian roulette when they terminate a dealer. It is for this reason that Sharp, although it prevailed below, does not oppose the petition and respectfully disagrees with the views expressed by the government with respect to the petition.

2. Despite the Court's invitation, the government's brief expresses no views with respect to the cross-petition. This decision was based solely upon the appropriations rider, which prohibits the Department of Justice from "engaging in activity to alter the *per se* prohibition on resale price maintenance . . . ." U.S. Br. 15. That stat-

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[1] The carefully crafted, precatory nature of the government's assurances on this critical issue illustrates the wisdom of Judge Jones' observation, concurring below, that "[s]emantic nuances are costly to businessmen in the real world." Pet. App. 22a.

ute, of course, did not preclude the Solicitor General from saying (a) that certiorari should be denied because the issue is not certworthy, or (b) that should certiorari be granted, the *per se* prohibition on vertical price fixing ought to be confirmed by the Court. Since the government said neither of these things, there can be little doubt as to the position the government would have taken on the cross-petition but for the appropriations rider.

This is particularly evident because the United States is already firmly on record as supporting review and reversal of the *per se* rule against resale price maintenance. In 1983, as *amicus curiae* in *Monsanto*, the United States urged this Court to "grant review . . . to consider whether *all* vertical restrictions, including resale price maintenance, should be analyzed under the rule of reason." [2] Brief for the United States as Amicus Curiae on Petition for a Writ of Certiorari at 13 (emphasis in original). It did so even though none of the parties in *Monsanto* had raised the issue at trial, or on appeal, or before this Court. The United States believed that review was appropriate notwithstanding the failure of the parties to preserve or present the issue, because the question was of such overarching importance and the application of the *per se* rule to vertical price restraints was so ill advised. *Id.* at 13-17.

It is equally clear that the government's views have not changed since *Monsanto*. On April 23, 1987, in testi-

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[2] The government's brief in support of the petition in *Monsanto* also noted:

> [T]he similarities in purpose and effect between resale price maintenance and non-price vertical restrictions led Justice White to observe in his concurring opinion in *Sylvania* that the "effect * * * of the Court's opinion is necessarily to call into question" the per se rule against the resale price maintenance. 433 U.S. at 70.

Brief for the United States as Amicus Curiae on Petition for a Writ of Certiorari at 15 n.22.

mony before the Subcommittee on Antitrust, Monopoly and Business Rights of the Senate Judiciary Committee, Acting Assistant Attorney General Charles F. Rule delivered as ringing an endorsement of Sharp's position as words allow:

> The Department of Justice filed a brief as amicus curiae in the *Monsanto* case expressing serious doubts as to the continued legitimacy of the current per se rule. We invited the Supreme Court to reexamine the rule, urging that resale price maintenance usually will not be used by a manufacturer simply to increase the retail price of its product, since it can do that more directly by raising its wholesale price. Rather, resale price maintenance usually will be designed to promote interbrand competition by encouraging dealers, *inter alia*, to train sellers, to undertake effective sales promotions, to create attractive showrooms, and to support informational, maintenance or repair services. Resale price maintenance curtails "free rider" dealers, who sell at discount prices to customers attracted to a product by other dealers' advertising or other promotional activities and who thus thwart procompetitive efforts desired by the manufacturer. Economists have posited several other procompetitive explanations of resale price maintenance as well.
>
> * * * *
>
> For the reasons articulated in our *Monsanto* brief, we view resale price maintenance agreements as potentially procompetitive—not just competitively neutral—in many circumstances.

Rule testimony at 6-7.

The specific statements made by the United States in *Monsanto* are worth repeating, both because these views were set forth prior to the interdiction of the appropriations statute and because Acting Assistant Attorney General Rule has confirmed that these views have not changed:

> [T]he logic of *Sylvania* compels the conclusion that resale price maintenance—like other vertical restrictions—is unsuitable for per se treatment.
>
> * * * *
>
> This Court has always regarded the rule of reason as the normal test of the legality of an alleged restraint: per se rules are invoked only where economic and judicial experience have shown that certain practices invariably have a "pernicious effect on competition" and lack "any redeeming [competitive] virtue." *Sylvania*, *supra*, 433 U.S. at 49-50; . . . . Accordingly, a per se rule against resale price maintenance can be justified only if there is some persuasive basis for supposing that the practice reduces output, retards innovation, or otherwise interferes with Sherman Act goals. But the Court has never analyzed resale price maintenance in terms of its actual economic effects, much less found that those effects are so necessarily anticompetitive as to justify a per se ban. Such an analysis would show that resale price maintenance, like the non-price vertical restrictions in *Sylvania*, can have significant procompetitive effects.

Brief for the United States as Amicus Curiae at 19, 20-21 (footnote omitted).

Other representatives of the government, when unfettered by the restrictions of the appropriations statute, have been equally emphatic in support of Sharp's position. Chairman Oliver of the Federal Trade Commission publicly stated that application of the rule holding vertical price restraints *per se* injurious to competition reflects an "ancient myth" that has been thoroughly debunked as a matter of economic doctrine. He further suggested that this case is the appropriate vehicle for this Court to resolve whether the *per se* rule should be eliminated in the vertical context. D. Oliver, Address to the Antitrust Law Section of the American Bar Association (Aug. 12, 1986), reprinted in 5 Trade Reg. Rep. (CCH) ¶ 50,481 at 56,287-88.

The continuity of the government's views over the four years since they were first espoused in *Monsanto* is hardly surprising. The proper treatment of vertical price fixing is the principal unresolved antitrust question of the day, and judicial and economic experience since *Monsanto* amply confirms the government's conclusion that the rule of reason, rather than the *per se* rule, is the appropriate standard of analysis. See authorities cited at Cross-Pet. 6-8. The government's unwillingness to address the issue, even in response to this Court's invitation, should be taken for what it obviously is: an acknowledgment that were it free to speak, it would again urge this Court to review the question of whether vertical price restraints should be subject to the *per se* rule, and then, on the merits, to resolve that question in the negative.[3]

3. Although Sharp believes that the proper treatment of vertical price restraints is so important that it would be appropriate to grant the cross-petition even if the petition were not deemed substantial, see *Snepp* v. *United*

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[3] The only reason offered by the government why certiorari might not be warranted is that this case is "interlocutory." See U.S. Br. 6 & n.7, 14. This contention is incorrect. No further proceedings would be required on remand if this Court either granted the petition and agreed with BEC's submission or granted the cross-petition and agreed with Sharp's submission. In the first instance, the judgment entered on the jury's verdict would simply be reinstated. In the latter instance, the complaint would have to be dismissed because BEC never sought to proceed below under a rule of reason theory and no such claim could have been established on this record. See Cross-Pet. 3-4.

In any event, even if the government's contention were correct, that would not be a reason to deny review here. This Court has not hesitated to grant review of important and unresolved antitrust issues, even though the judgment below was interlocutory. See, *e.g.*, *Matsushita Electric Industrial Co.* v. *Zeneth Radio Corp.*, 106 S.Ct. 1348 (1986). As we explain in the text, it is essential that the business community know the rules governing vertical price restraints. Nothing that can occur on remand in this case can dispel the current confusion on that issue.

States, 444 U.S. 507, 524-25 (1980) (Stevens, J., dissenting), both the petition and the cross-petition present questions that plainly are "certworthy" under the traditional standards applied by this Court. These questions are frequently recurring ones of immense practical importance on which there exists a direct conflict among the circuits. The legal issues are well-focused, and they have been properly preserved for this Court's review. Finally, the record in this case presents all of the factual and economic information needed to support an in-depth analysis by the Court.

Accordingly, certiorari should be granted to review the questions presented by the petition and cross-petition.

Respectfully submitted.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

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v.

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SHARP ELECTRONICS CORPORATION,
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v.

BUSINESS ELECTRONICS CORPORATION

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

SUPPLEMENTAL BRIEF FOR PETITIONER PURSUANT TO RULE 22.6

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This supplemental brief is submitted in reply to the brief filed by the United States as *amicus curiae*.

1. *Monsanto* Did Not Decide This Case.

Quite unlike the issue decided in *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), the petition of Business Electronics Corporation ("BEC") raises the question whether the admittedly collusive termination of a dealer for the purpose of reducing price competition constitutes a per se violation of the Sherman Act. While *Monsanto* addressed the element of conspiracy in a vertical price fixing case, this petition goes the next step and raises the question of conspiracy to do what. By its decision below, the Fifth Circuit rewrote decades of established antitrust jurisprudence by holding that a concerted decision to eliminate a price cutting dealer is not per se unlawful unless it is accompanied by a finding of an express agreement on price.

The Solicitor General misreads *Monsanto*. That decision arose from a dispute in the circuit courts over the type of proof required to establish an inference of conspiracy in a vertical price fixing action. *See id.* at 758-59 and n. 5. The Court resolved that conflict by rejecting the "complaints followed by termination" and the "termination in response to complaints" tests and adopting a standard requiring "evidence that tends to exclude the possibility that the manufacturer and nonterminated distributors were acting independently." *Id.* at 764. Of the two important distinctions in vertical antitrust cases recognized in *Monsanto*, it was the first one, between concerted and independent action, which was addressed by the Court.

The jury finding of concerted action to eliminate BEC was not questioned by Sharp or the Fifth Circuit, even in light of the *Monsanto* standard. Instead, that court held that collusive termination of a dealer to reduce price competition is a per se violation only if there is an additional, express finding of a direct agreement on resale prices. *Business Electronics Corp. v. Sharp Electronics Corp.*, 780 F.2d 1212, 1216 (5th Cir. 1986).

2. *Monsanto* Has Not Abated the Conflict in the Courts of Appeals.

Because the Court was not presented with this question in *Monsanto*, it is not surprising that *Monsanto* has not abated the pronounced conflict in the circuits. As discussed in the supplemental brief filed by Sharp, the standard for determining a per se unlawful vertical price fixing agreement continues to vary widely by geography.

Accordingly, certiorari should be granted to review the question presented by BEC's petition, and, for the reasons discussed in BEC's brief in opposition to Sharp's cross-

petition, certiorari should be denied to Sharp's cross-petition.

Respectfully submitted,

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CERTIFICATE OF SERVICE

This is to certify that on this the 1st day of June, 1987, a true and correct copy of the above and foregoing instrument was forwarded by certified mail, return receipt requested to the following counsel of record:

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Nos. 85-1910 and 85-2094

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OCTOBER TERM, 1986

BUSINESS ELECTRONICS CORPORATION, PETITIONER

v.

SHARP ELECTRONICS CORPORATION

SHARP ELECTRONICS CORPORATION, CROSS-PETITIONER

v.

BUSINESS ELECTRONICS CORPORATION

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

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QUESTIONS PRESENTED

1. Whether a supplier's decision to terminate a retailer for cutting prices is a per se violation of Section 1 of the Sherman Act, 15 U.S.C. 1, only when it is the product of an agreement to maintain resale prices.

2. Whether this Court should reconsider its determination (see *Dr. Miles Medical Co.* v. *John D. Park & Sons,* 220 U.S. 373 (1911)) that resale price maintenance is per se unlawful under Section 1 of the Sherman Act.

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In the Supreme Court of the United States

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No. 85-1910

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BUSINESS ELECTRONICS CORPORATION

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

This brief is submitted in response to the Court's order inviting the Solicitor General to express the views of the United States.

STATEMENT

1. Sharp Electronics Corporation distributes a variety of consumer and business products, including electronic calculators, to retail dealers who resell these products to end users. Sharp publishes a list of suggested minimum

retail prices for its products. Pet. App. 5a.[1]

In 1968, Business Electronics Corporation (BEC) became the exclusive retailer of Sharp calculators in the Houston, Texas area. Sharp subsequently became dissatisfied with BEC's performance. Sharp claimed that its dissatisfaction was due to BEC's failure to meet sales quotas; BEC claimed that Sharp was unhappy with BEC's policy of selling Sharp calculators at prices lower than Sharp's suggested resale prices. Pet. App. 5a.

In 1972, Sharp appointed Gilbert Hartwell as a second retail dealer in the Houston area. Although Sharp's local sales representative led Hartwell to believe that his dealership would be exclusive, Sharp's national sales manager was unwilling to terminate BEC's dealership without personally evaluating BEC's performance. Pet. App. 5a; Tr. 272, 1307-1308. BEC and Hartwell competed for approximately one year, each selling Sharp products in the Houston market. Hartwell complained both to the owner of BEC and to Sharp about BEC's discounting practices during this period.[2] In June 1973, Hartwell informed Sharp that he would terminate his dealership unless Sharp ended its relationship with BEC within 30 days. Sharp terminated BEC's dealership in July 1973. Pet. App. 6a.

2. BEC subsequently commenced this action in the United States District Court for the Southern District of Texas, asserting that Sharp's treatment of BEC violated Section 1 of the Sherman Act, 15 U.S.C. 1. The complaint alleged that Sharp had "conspired to require retail price maintenance"; that BEC "refused to abide by these requirements"; and that, as a resuit, Sharp discontinued

[1] "Pet. App." references are to the appendix to the petition in No. 85-1910.

[2] Hartwell himself did not always adhere to Sharp's schedules of suggested resale prices and testified that he was under no obligation to do so. Pet. App. 6a.

its relationship with BEC. First Amended Complaint ¶ V(b).[3]

The district court instructed the jury, over Sharp's objection, that the Sherman Act is violated " 'when a seller enters into an agreement or understanding with one of its dealers to terminate another dealer because of the other dealer's price cutting' " (Pet. App. 6a). The jury was asked to decide, pursuant to a special interrogatory, whether " 'there was an agreement or understanding between Sharp and Hartwell to terminate Business Electronics as a Sharp dealer because of Business Electronics' price-cutting' " (*id.* at 7a). The jury returned a verdict in BEC's favor and answered "yes" to the special interrogatory.

The district court denied Sharp's motion for judgment notwithstanding the verdict or, in the alternative, a new trial (Pet. App. 24a-34a). The court rejected Sharp's argument that the legality of its conduct under Section 1 should have been measured by the rule of reason (*id.* at 27a). It further found that "there was sufficient evidence for the jury to have concluded that Sharp and Hartwell were parties to an agreement to set product retail prices and, in furtherance of that agreement, that BEC was terminated for refusing to adhere to those prices" (*id.* at 28a-29a).[4]

3. The court of appeals reversed (Pet. App. 1a-19a). It stated that in order to invoke the per se rule against resale price maintentance "it was not enough for the jury to find that BEC was terminated to reduce price competition; the

[3] BEC also alleged that Sharp's "territorial restrictions" violated Section 1 of the Sherman Act. First Amended Complaint ¶ V(a). BEC apparently abandoned that claim following this Court's decision in *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

[4] The court also rejected Sharp's assertion that there was not sufficient evidence to support the award of damages (Pet. App. 29a-30a), its claim that the jury instructions were erroneous (*id.* at 30a-32a), and its challenges to certain evidentiary rulings (*id.* at 32a-34a).

jury should have been required to find that the termination was pursuant to a price maintenance agreement between Sharp and Hartwell" (*id.* at 7a-8a). The court of appeals observed that this Court in *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984), had distinguished between "concerted action to set prices and concerted action on non-price restrictions—the former is illegal *per se* while the latter is evaluated under the rule of reason" (Pet. App. 10a). It found that "the language of *Monsanto* can only indicate the [Supreme] Court's belief that a price fixing agreement is a requirement for *per se* liability in distributor-termination cases" (*id.* at 13a). The court of appeals concluded that, "in order for a manufacturer's termination of a distributor to be illegal *per se,* it must be pursuant to a price maintenance agreement with another distributor. That distributor must expressly or impliedly agree to set its prices at some level, though not a specific one. The distributor cannot retain complete freedom to set whatever price it chooses" (*id.* at 13a-14a). Because the jury instructions "failed to reflect this standard," the court found that they were "critically defective" (*id.* at 14a (footnote omitted)).

The court of appeals went on to reject Sharp's claim that there was insufficient evidence to raise a jury issue regarding the existence of a price maintenance agreement between Sharp and Hartwell. "While it is true that there was little, if any, direct evidence that Sharp and Hartwell reached an agreement as to price," the court stated, "we think the jury reasonably could infer such an agreement from the evidence as a whole" (Pet. App. 15a). The court remanded the case for further proceedings consistent with its opinion.[5]

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[5] The court also addressed several evidentiary issues raised by Sharp (Pet. App. 15a-18a) and upheld the method of calculation of damages utilized by the district court (*id.* at 18a).

Judge Jones filed a separate concurring opinion (Pet. App. 19a-23a). She stated that "this case perfectly illustrates the arguments why vertical price restraints should be tested under antitrust's Rule of Reason rather than, as *Monsanto* continues to require, per se illegality. * * * [A]lthough *Monsanto* moves toward alleviating the threat of unwarranted treble-damage action, the abiding uncertainty suggests that the Supreme Court would more wisely jettison the precedent that led to the rule of per se illegality for vertical price restraints" (*id.* at 19a (footnote omitted)).

DISCUSSION

1. This case brings before the Court the issue that it considered most recently in *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984): the proper analysis under Section 1 of the Sherman Act, 15 U.S.C. 1, of a supplier's decision to terminate a wholesaler or retailer. The Court observed in *Monsanto* that one "important distinction[] * * * at the center of * * * any * * * distributor-termination case" is the distinction "between concerted action to set prices and concerted action on nonprice restrictions" (465 U.S. at 760-761).[6] Concerted action to set prices "ha[s] been *per se* illegal since the early years of national antitrust enforcement"; nonprice restrictions, on the other hand, "are judged under the rule of reason, which requires a weighing of the relevant circumstances of a case to decide whether a restrictive practice constitutes an unreasonable restraint on competition" (*id.* at 761).

The question presented in the petition in No. 85-1910 concerns the dividing line between these two types of vertical restraints. The jury found an agreement between a supplier and one of its retailers to terminate a second retailer because of price cutting; the jury was not instructed that in order to return a verdict for plaintiff it had

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[6] A second distinction identified by the Court in *Monsanto*—the one between concerted action and independent action—is not relevant in this case.

to find an agreement to set prices. We agree with the court of appeals that the agreement the jury found—standing alone—is not per se unlawful. The per se rule would apply only if the termination of the retailer were shown to be the product of an agreement to set resale prices. Although there has been some disagreement among the courts of appeals with respect to this question, the decisions since this Court's decision in *Monsanto* are generally in accord with the view adopted by the court below. Review by this Court of the interlocutory question presented in No. 85-1910 is therefore not warranted.[7]

a. A practice is deemed per se unlawful under Section 1 of the Sherman Act, 15 U.S.C. 1, only when experience indicates that the conduct has a "pernicious effect on competition and lack[s] any redeeming virtue." *Northern Pacific Railway* v. *United States*, 356 U.S. 1, 5 (1958); see also *Broadcast Music, Inc.* v. *CBS, Inc.*, 441 U.S. 1, 8 (1979). "The decision to apply the *per se* rule turns on 'whether the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output * * * or instead one designed to "increase economic efficiency and render markets more, rather than less, competitive." ' " *Northwest Wholesale Stationers, Inc.* v. *Pacific Stationery & Printing Co.*, 472 U.S. 284, 289-290 (1985), quoting *Broadcast Music, Inc.* v. *CBS, Inc.*, 441 U.S. at 19-20.

Price fixing among competitors is "perhaps the paradigm of an unreasonable restraint of trade." *NCAA* v. *Board of Regents*, 468 U.S. 85, 100 (1984) (footnote

[7] The court of appeals' decision permits BEC to argue on remand that Sharp's actions were per se unlawful. Conduct not per se unlawful may be unlawful under a rule of reason analysis. See *Standard Oil Co.* v. *United States*, 221 U.S. 1, 62 (1911). We express no view on whether BEC has preserved such a contention.

omitted); see also *Catalano, Inc.* v. *Target Sales, Inc.*, 446 U.S. 643, 647 (1980) (per curiam). In the horizontal context, an agreement to eliminate price competition generally serves no procompetitive purpose: it usually reduces consumer welfare if the collaborators have market power, and it rarely serves legitimate objectives. See 2 P. Areeda & D. Turner, *Antitrust Law* § 314, at 47 (1978). Thus, per se condemnation attaches to a wide variety of price-related agreements among competitors, including agreements that only indirectly affect price. *Catalano, Inc.* v. *Target Sales, Inc.*, 446 U.S. at 647-648 (noting the variety of horizontal arrangements condemned as per se illegal price-fixing); 2 J. von Kalinowski, *Antitrust Laws and Trade Regulation* § 6A.02[1], at 6A-9 to 6A-13 (1986).[8]

With respect to vertical agreements, the Court has painted with a narrower brush.[9] The Court has consistently adhered to the view that resale price maintenance—a vertical agreement to set prices—constitutes a per se violation of Section 1. See, *e.g.*, *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc.*, 445 U.S. 97, 102-103 (1980); *United States* v. *Parke, Davis & Co.*, 362 U.S. 29, 38-45 (1960); *Dr. Miles Medical Co.* v. *John D. Park & Sons*, 220 U.S. 373, 407 (1911). This brief does not

[8] Even in the context of horizontal price-fixing, however, this Court has cautioned that "easy labels do not always supply ready answers" (*Broadcast Music, Inc.* v. *CBS, Inc.*, 441 U.S. at 8). Some horizontal arrangements that have an impact on price, such as mergers and joint ventures, are neither per se violations nor unreasonable restraints (*id.* at 23). Indeed, some horizontal combinations that literally "fix prices" have been held not to be per se illegal "price-fixing" because they " 'render[ed] markets more, rather than less, competitive.' " *Id.* at 19-20, quoting *United States* v. *United States Gypsum Co.*, 438 U.S. 422, 441 n.16 (1978); see also *NCAA* v. *Board of Regents*, 468 U.S. at 107.

[9] A vertical agreement is one involving firms at different levels of the market structure. For example, an agreement between a wholesaler and a retailer is a vertical agreement.

seek to alter that rule (see pages 14-15, *infra*). Nonprice vertical restraints, on the other hand, are governed by the rule of reason. *Monsanto,* 465 U.S. at 763; *Continental T.V., Inc. v. GTE Sylvania, Inc.,* 433 U.S. 36 (1977). Thus, "it is of considerable importance that * * * concerted action on nonprice restrictions, be distinguished from price-fixing agreements, since under present law the latter are subject to *per se* treatment and treble damages" (*Monsanto,* 465 U.S. at 763).

This Court has applied the per se rule against resale price maintenance only to situations in which the evidence showed that the manufacturer or wholesaler "dictat[ed] the prices charged by" a wholesaler or retailer. *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc.,* 445 U.S. at 103; see also *324 Liquor Corp.* v. *Duffy,* No. 84-2022 (Jan. 13, 1987), slip op. 5-6; *Albrecht* v. *Herald Co.,* 390 U.S. 145, 149-150 (1968); *United States* v. *Parke, Davis & Co.,* 362 U.S. at 45-46; *Schwegmann Brothers* v. *Calvert Corp.,* 341 U.S. 384, 385-386 (1951); *Kiefer-Stewart Co.* v. *Joseph E. Seagram & Sons,* 340 U.S. 211, 212-213 (1951); *United States* v. *A. Schrader's Son, Inc.,* 252 U.S. 85 (1920); *Dr. Miles Medical Co.* v. *John D. Park & Sons,* 220 U.S. at 394. In *Monsanto,* the Court found the evidence sufficient to establish a resale price maintenance conspiracy because the evidence showed "that Monsanto and some of its distributors were parties to an 'agreement' or 'conspiracy' to *maintain resale prices* and terminate price cutters." 465 U.S. at 765 (emphasis added); see also *id.* at 764 n.9 (to show the requisite agreement, "evidence must be presented both that the distributor communicated its acquiescence or agreement [to the suggested price], and that this was sought by the manufacturer"). Under this Court's decisions, therefore, the per se rule may only be invoked upon a showing that the wholesaler or retailer has ceded to its supplier some or all control over its pricing decisions. See Pet. App. 14a.

If the Court does not distinguish between the quite different problems presented by horizontal and vertical price fixing, "there is a considerable danger that the doctrine[] enunciated in [*Continental T.V., Inc.* v. *GTE Sylvania, Inc., supra*] * * * will be seriously eroded" (*Monsanto,* 465 U.S. at 763). The Court concluded in *Sylvania* that nonprice vertical restraints should be assessed under the rule of reason because such restraints potentially "promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products" (433 U.S. at 54). For example, new entrants into a market may use vertical restrictions "to induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer" (*id.* at 55). An established manufacturer may impose restrictions on intrabrand competition in order to encourage retailers to provide services and facilities necessary to efficient marketing of the product (*ibid.*). Such vertical restraints encourage retailers to offer such services because they eliminate the possibility of "free-riding" by retailers who do not offer such services and who, as a consequence, are able to charge lower prices. See *Monsanto,* 465 U.S. at 762-763.[10]

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[10] Services such as providing presale information and post-sale repair facilities may affect the competitiveness of a manufacturer's product. (*Sylvania,* 433 U.S. at 55). Moreover, a manufacturer may determine that its product is most competitive with other brands when these services are offered without separate charge to the consumer. In order to persuade dealers to offer such services, manufacturers must either compensate the dealers directly or otherwise enable the dealers to earn the higher gross margins necessary to defray the cost of the services. Otherwise, dealers offering "free" ancillary services will have their prices undercut by, and lose sales to, dealers who have lower costs because they offer no such services. *Ibid.*; see also *Beach* v. *Viking Sewing Machine Co.,* 784 F.2d 746, 751 n.6 (6th Cir. 1986). The prospect of "free-riding" by some dealers on the promotional and

The Court observed in *Sylvania* that vertical restraints "reduce intrabrand competition by limiting the number of sellers of a particular product competing for the business of a given group of buyers" (433 U.S. at 54). That is, many nonprice vertical restraints protect sellers from price competition. The "location clause" held subject to rule of reason scrutiny in *Sylvania,* for example, was designed to insulate a dealer from the price and nonprice competition that he would face if other dealers were free to establish new locations. Indeed, to the extent that vertical restrictions succeed in encouraging dealer efforts, and thereby strengthen a product's competitive position, they do so precisely because they allow dealers to charge prices that cover the costs of providing the extra services that the manufacturer deems necessary for the efficient distribution of the product.[11]

Accordingly, a vertical restraint cannot be per se unlawful merely because it reduces intrabrand price competition: such an effect is a characteristic of *both* resale price maintenance and nonprice restraints. Indeed, this Court observed in *Monsanto* that the "economic effect" of price and nonprice restrictions is "in many, but not all, cases similar or identical." 465 U.S. at 762; see also

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educational services of other dealers diminishes the incentives of dealers generally to offer these services in amounts necessary to ensure effective product distribution. As a result, fewer of the manufacturer's products find their way into the market—to the detriment of consumers.

[11] Vertical restrictions that lead to increased retail prices will be unprofitable for the manufacturer unless they also increase dealer sales. See *Sylvania,* 433 U.S. at 56 n.24 (citing authorities) (a manufacturer generally would prefer the lowest retail prices possible in order to increase sales and manufacturer revenues). If dealers increase their prices without providing ancillary services valued by consumers, sales would decrease as consumers turn to competing brands or decide not to purchase the product.

Sylvania, 433 U.S. at 69-70 (White, J., concurring in the judgment). Treating any reduction in price competition as justifying application of the per se rule would result in the application of the per se rule to virtually all vertical restraints, contrary to this Court's decisions in *Sylvania* and *Monsanto.* The per se rule has been restricted to those situations in which a seller has ceded to his supplier some of his authority to set prices.[12]

These general principles were properly applied by the court of appeals in this case. An agreement to eliminate a competing dealer, like other nonprice vertical restraints, may reduce intrabrand price competition.[13] Precisely for that reason, such an agreement may serve the legitimate purpose of allowing dealers to charge prices that cover the cost of services necessary to the efficient distribution of the product. Sharp contended here, for example, that BEC was free-riding on Hartwell's investment in product pro-

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[12] BEC contends (85-2094 Br. in Opp. 11-12) that the adoption by Congress of a resolution (see Pub. L. No. 99-180, § 605, 99 Stat. 1169-1170) criticizing in certain respects the Vertical Restraints Guidelines issued by the Antitrust Division of the Department of Justice (see 50 Fed. Reg. 6265-6266 (1985)) undercuts the court of appeals' conclusion regarding the scope of the per se rule. But the guidelines' definition of the per se rule is narrower than the definition adopted by the court of appeals—the guidelines state that the per se rule applies only where "there is direct or circumstantial evidence (other than effects on price) establishing an explicit agreement as to the specific prices at which goods or services would be resold" (*ibid.*). Congress criticized that narrow rule (see § 605, 99 Stat. 1169); it did not express a view regarding the somewhat broader rule adopted by the court of appeals. See generally *Consumer Product Safety Comm'n* v. *GTE Sylvania, Inc.*, 447 U.S. 102, 117-118 (1980); *United States* v. *Philadelphia National Bank*, 374 U.S. 321, 348-349 (1963).

[13] Indeed, such an agreement is similar in this respect to the system of exclusive territories at issue in *Sylvania.* In each case, the dealer is insulated from price competition.

motion and other sales-related services. As the court of appeals concluded, a vertical agreement to restrict intrabrand price competition by eliminating a discounting dealer—without prescribing the level of the remaining dealer's resale prices—may " 'increase economic efficiency and render markets more, rather than less, competitive.' " *Northwest Wholesale Stationers, Inc.*, 472 U.S. at 295, quoting *Broadcast Music, Inc.*, 441 U.S. at 20. Such a restraint is therefore properly evaluated under the rule of reason.

b. Although the decisions of other courts of appeals rendered prior to this Court's decision in *Monsanto* appear to conflict with the decision below, the conflict has largely abated as a result of subsequent developments in those circuits. In view of the strong trend toward adoption of the rule espoused by the court below, review by this Court is not warranted at this time.

When it rendered its decision in this case, the court of appeals stated that four other circuits had adopted a conflicting rule. See Pet. App. 8a, citing *Cernuto, Inc.* v. *United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979); *Bostick Oil Co.* v. *Michelin Tire Corp.*, 702 F.2d 1207, 1215 (4th Cir.), cert. denied, 464 U.S. 894 (1983); *Victorian House, Inc.* v. *Fisher Camuto Corp.*, 769 F.2d 466 (8th Cir. 1985) (post-*Monsanto* decision); *Zidell Explorations, Inc.* v. *Conval International, Ltd.*, 719 F.2d 1465 (9th Cir. 1983). The Fourth and Eighth Circuits appear to have subsequently abandoned their prior position and endorsed the rule applied by the court of appeals in the present case. See *Garment District, Inc.* v. *Belk Stores Services, Inc.*, 799 F.2d 905, 908-909 (4th Cir. 1986); *McCabe's Furniture, Inc.* v. *La-Z-Boy Chair Co.*, 798 F.2d 323, 329-330 (8th Cir. 1986).[14] Other courts of appeals have

[14] Both decisions cite and follow *Monsanto*. Neither court referred to its prior decisions.

also adopted the rule espoused by the court below. *Bender* v. *Southland Corp.*, 749 F.2d 1205, 1212 (6th Cir. 1984); *Morrison* v. *Murray Biscuit Co.*, 797 F.2d 1430, 1440 (7th Cir. 1986); *Westman Comm'n Co.* v. *Hobart International, Inc.*, 796 F.2d 1216, 1223-1224 (10th Cir. 1986); see also *Borger* v. *Yamaha International Corp.*, 625 F.2d 390, 396-398 (2d Cir. 1980).

The Third and Ninth Circuits—the other circuits identified by the court of appeals and petitioner as adopting a rule different from that applied by the court below—have not had occasion to revisit the issue since this Court's decision in *Monsanto*. Like the other courts of appeals, these courts may well conclude that this Court's decision in *Monsanto* requires the modification of the rule announced in their prior decisions.[15] For that reason, we suggest that review by this Court is not warranted.

[15] The Ninth Circuit's decision in *Zidell* was cited in *O.S.C. Corp.* v. *Apple Computer, Inc.*, 792 F.2d 1464 (9th Cir. 1986). The court in that case found the evidence insufficient to establish a per se violation principally because of the absence of proof of conspiracy (see 792 F.2d at 1467, 1468-1469); it therefore had no occasion to consider the precise scope of the per se rule. It is noteworthy that the court of appeals did support its conclusion that the per se rule did not apply by stating that "[t]here was no evidence [the manufacturer] coerced dealers on advertising or pricing decisions. The dealers admitted that [the manufacturer's] suggested retail prices were not binding" (*id.* at 1469). Indeed, in *49er Chevrolet, Inc.* v. *General Motors Corp.*, 803 F.2d 1463 (9th Cir. 1986), the Ninth Circuit, rejecting a claim by General Motors dealers that GM had engaged in per se vertical price-fixing by imposing on them prices for repairs of damaged vehicles, stated that "allegations of vertical price-fixing are generally evaluated under the 'rule of reason' " (803 F.2d at 1468).

Following this Court's decision in *Monsanto*, the Third Circuit has cited its decision in *Cernuto* for principles of law not relevant here—the standard for granting summary judgment in Section 1 cases and the test for determining whether a complaining dealer's allegations of concerted action are sufficient to defeat summary judgment; it has not applied *Cernuto* to identify the type of conduct that falls within the per

2. The question presented in the cross-petition (No. 85-2094) is whether the Court should reconsider its decisions holding that resale price maintenance is per se unlawful. We note preliminarily that the question presented in the cross-petition (like the question presented in the petition) is interlocutory: a properly instructed jury may conclude on remand that Sharp did not engage in resale price maintenance. Moreover, should the Court conclude that certiorari is not appropriate with respect to the question presented in the petition in No. 85-1910, Sharp would be in the posture of cross-petitioning from a favorable judgment on the ground that it won a less complete victory in the court of appeals than it believes to be appropriate.

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se prohibition against resale price maintenance. *Arnold Pontiac-GMC, Inc.* v. *General Motors Corp.*, 786 F.2d 564, 572-574 (3d Cir. 1986); *Seaboard Supply Co.* v. *Congoleum Corp.*, 770 F.2d 367, 374 (3d Cir. 1985); *Tunis Bros.* v. *Ford Motor Co.*, 763 F.2d 1482, 1497-1501 (3d Cir. 1985), vacated, No. 85-487 (Apr. 7, 1986); *Fragale & Sons Beverage Co.* v. *Dill*, 760 F.2d 469, 473-474 (3d Cir. 1985); *Malley-Duff & Associates* v. *Crown Life Ins. Co.*, 734 F.2d 133 (3d Cir.), cert. denied, 469 U.S. 1072 (1984).

Upon a close review of the *Cernuto* and *Zidell* decisions, moreover, it is by no means clear that they would present a clear conflict with the Fifth Circuit's decision in this case even if those circuits were to adhere to those decisions after *Monsanto*. The courts in both cases stated that the per se rule would not apply if a supplier were shown to have acted pursuant to a legitimate business purpose. See 595 F.2d at 170 (emphasis added) ("if defendants can demonstrate that their actions were not motivated *solely* by considerations of price then the use of a *per se* rule might be inappropriate"); 719 F.2d at 1471 (jury must be instructed to determine "whether any of the supplier's asserted motives were an actual, bona fide pursuit of a legitimate business purpose" before deciding whether to classify the conduct as illegal per se). Even in these courts' view, therefore, proof that *one* of the purposes of a vertical agreement was to reduce price competition would not be sufficient to invoke the per se rule. Indeed, the broader inquiry required under these decisions makes the analysis applied by these courts more akin to a rule of reason test than to a rule of per se illegality.

Apart from these observations, we express no view on the merits of the issue presented in the cross-petition (No. 85-2094) or on the suitability of that issue for review by this Court. The statute appropriating funds for the operation of the Department of Justice during the current fiscal year states in pertinent part that "[n]one of the funds appropriated in * * * this Act may be used for any activity to alter the per se prohibition on resale price maintenance in effect under Federal antitrust laws" (Pub. L. No. 99-591, § 605, 100 Stat. 3341-73).[16] The President has questioned the constitutionality of this restriction upon the authority of the Executive Branch to "take Care that the Laws be faithfully executed" (Art. II, § 3, Cl. 4) as well as the wisdom of addressing important substantive issues through restrictions on government expenditures. See *Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriations Act, 1984*, 19 Weekly Comp. of Pres. Doc. 1619 (Dec. 5, 1983). Nonetheless, to avoid raising the constitutional question here, we have decided to abide by the wishes of Congress in responding to the Court's invitation. Because our determination places off limits some of the possible answers to the Court's inquiry, and because we believe that the Solicitor General should not undertake to advise the Court on a question to which some possible answers are thus precluded, we respectfully decline to express any view on the question presented in the cross-petition.

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[16] The provision exempts from this limitation the expenditure of funds in connection with testimony before Congress.

CONCLUSION

The petition for a writ of certiorari in No. 85-1910 should be denied. We express no opinion regarding the appropriate disposition of the petition in No. 85-2094.

Respectfully submitted.

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NO. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

JOINT APPENDIX

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PETITION FOR CERTIORARI FILED MAY 21, 1986

CERTIORARI GRANTED JUNE 8, 1987

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UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS

Civil Action No. H-78-1020

Business Electronics Corporation and
Kelton Ehrensberger, an individual d/b/a
Electronic Business Machines,
Plaintiffs,

v.

Sharp Electronics Corporation,
Defendant.

RELEVANT DOCKET ENTRIES

DATE—NR.—PROCEEDINGS

6-7-78—Received the following filed instruments from WD of Tx., San Antonio Div., SA-76-CA-49, as follows:

7-11-75—Complaint, filed. (3) summons issued.

5-15-78—Motion for Leave to File Amended Complaint and for Transfer to Southern District of Texas, filed.

6-5-78—FILE TRANSFERRED TO SOUTHERN DISTRICT OF TEXAS, HOUSTON DIVISION.

2-11-82—(GKMc) ORDER, filed. Parties ntfd. aa

1. The first Amended comp. is deemed to have been filed with leave of court in its entirety.

2. The damage allegation in the first amended comp. is deemed to be $1,245,000 instead of $500,000. Pltfs. need not file any other amendment.

3. The amendments in the first amended comp. relate back to the filing of the orig. comp.

2-11-82—(GKMc) ORDER, filed. Parties ntfd. aa
1. Defts motion for summary judgment is DENIED.
2. Deft's motion to strike is DENIED.

10-11-83—JOINT SECOND AMENDED PRETRIAL ORDER, filed. fm

w/a. pltf's Requested voir dire questions
b. pltf's Proposed charge to jury
c. deft's Requested voir dire Instructions and Examination
d. deft's Requested jury instructions and special verdict
e. pltf's exhibit list
f. deft's exhibit list

10-17-83—(WS) 1ST DAY JURY TRIAL, filed . . .
Jury selected . . . Pltf. opening statement; deft. opening statement; Pltf. witness: Kelton Ehrensberger.

10-18-83—(WS) 2ND DAY JURY TRIAL, filed . . .
Pltf. witness: Kelton Ehrensberger, cont.
Adjourned to resume 10-19-83 at 10:00 a.m.

10-19-83—(WS) 3RD DAY JURY TRIAL, filed . . .
Pltf. witness: Gilbert Hartwell, testimony from deposition of Hitasake Nishitan.
Adjourned: to resume 10-20-83 at 10:00 a.m.

10-20-83—(WS) 4TH DAY JURY TRIAL, filed . . .
Pltf. witness: Joseph M. Chernow, testimony from deposition of Thomas George Mashos, testimony from deposition of Thomas Jesse Burkholder, Jr. adjourned. To resume on 10-24-83 at 10:00 a.m.

10-24-83—5TH DAY JURY TRIAL, filed . . .
Pltf. witness: Testimony from deposition of Thomas Jesse Burkholder, Jr. cont'd.
Pltf. rests.
(outside presence of jury) Deft. moves for directed verdict in favor of deft.—overruled. Deft. witness: Thomas Jesse Burkholder, Jr.
Adjourned: to resume 10-26-83 at 10:00 a.m.

10-26-83—6TH DAY JURY TRIAL, filed . . .
Testimony of Thomas Jesse Burkholder, Jr. cont'd. . .
Adjourned to resume 10-27-83 at 10:00 a.m.

10-27-83—7TH DAY JURY TRIAL, filed . . .
Testimony of Thomas Jesse Burkholder, Jr. cont'd.
Testimony of Gilbert Hartwell, Testimony of Thomas Jesse Burkholder, Jr. cont'd.
Adjourned to resume 10-28-83 at 10:00 a.m.

10-28-83—8TH DAY JURY TRIAL, filed . . .
Deft. witness: Steve Jizmagian;
Adjourned: to resume 10-31-83 at 10:00 a.m.

10-31-83—9TH DAY JURY TRIAL, filed . . .
Deft. witnesses cont'd: Gary Walther, testimony from deposition of Thomas George Mashos, testimony from deposition of Hiroshi Kawai. Adjourned to resume at 10:00 a.m. on 11-1-83.

11-1-83—10TH DAY JURY TRIAL, filed . . .
Pltf. cross-examination by reading testimony from deposition of Thomas George Mashos; pltfs. cross examination by reading testimony from deposition of Hiroshi Kawai; defts. redirect by reading testimony from deposition of Kiroshi Kawai. Deft. witness cont. Ira J. Tabanken; deft. adverse witness, Kelton Ehrensberger; Charles Leslie.
Pltf. rests, defts. rest. Adjourned to resume on Nov. 3, 83 at 10:00 a.m.

11-2-83—MOTION HEARING, Filed . . .
Deft. motion f/directed verdict on 1) liability, 2) Rule of Reason, 3) Per Se Theory, 4) Damages—Overruled.
Adjourned. To resume: Nov. 3, 1983 at 10:00 a.m.

11-3-83—11TH DAY JURY TRIAL, filed . . .
Pltf. opening arguments, defts. closing argument. Pltf. closing argument.
Jury charge—Alternate juror excused. (outside presence of jury) deft. makes objections to jury instructions—overruled. Jury deliberates.
Adjourned at 4 p.m. to resume deliberation 11-4-83 at 10:00 a.m.

11-4-83—12TH DAY JURY TRIAL, filed . . .
Jury deliberating. Verdict in favor of pltf.

11-30-83—Pltf. MOTION FOR ENTRY OF JUDGMENT, filed.

12-7-83—(WS) JUDGMENT, filed, Parties ntfd. . . The amended orders signed and entered Dec. 1, 83, are vacated. Pltf. recover of deft. Sharp Electronics the sum of $2,036,875.

12-19-83—Deft's MOTION FOR JUDGMENT NOTWITHSTANDING THE VERDICT, or in the Alternative, FOR A NEW TRIAL, filed.

1-9-84—Pltf's MEMORANDUM IN OPPOSITION to deft's motion for judgment notwithstanding the verdict or, in the alternative, for a new trial, filed.

9-28-84—(WS)—MEMORANDUM AND ORDER, filed. Parties ntfd.
1. Deft's Motion f/Judgment notwithstanding verdict, or for New Trial is DENIED.
2. This is a Final Judgment.

10-26-84—Deft. NOTICE OF APPEAL from the Final Judgment entered on Sept. 28, 1984, filed.

10-26-84—Filing & Docketing Fees Both paid #104033.

10-30-84—Record on Appeal consisting of All Original Papers (7 Vols.)
Exhibits (1 Expandable folder) Transcripts (15 Vols.) Depositions (17 Vols.) forward to the Court of Appeals.

10-31-84—Case Number 84-2618 docketed in the United States Court of Appeals for the Fifth Circuit.

1-21-86—Opinion of Court of Appeals Rendered. Reversed.

2-4-86—Appellee's Petition for Rehearing En Banc filed.

2-20-86—Order of Court of Appeals Denying Rehearing.

6-5-86—Notice of Flg. of Cert. Pet. on 5-21-86.

6-12-87—Order of S.C. Granted 6-8-87.

DEFENDANT'S EXHIBIT 121

IN THE
DISTRICT COURT OF THE UNITED STATES
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

CIVIL ACTION NO. H-78-1020

BUSINESS ELECTRONICS CORP., ET AL.,
Plaintiffs,

v.

SHARP ELECTRONICS CORPORATION,
Defendant.

DEFENDANT'S REVISED JURY INSTRUCTIONS AND SPECIAL VERDICT

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DEFENDANT'S REQUESTED JURY INSTRUCTION NO. 23

Necessity of Agreement on Price

In addition to finding an agreement between Sharp and Hartwell, you must also find that the agreement was to fix or maintain resale prices of Sharp calculators at a certain level and not just that the agreement may have had some effect on price. Not every agreement that has some effect on price is a price fixing agreement. Every decision a manufacturer makes necessarily affects the price of its product. For example, anytime a manufacturer terminates a dealer and replaces him with another dealer, or appoints an exclusive dealer—things perfectly legal under the antitrust laws—this may have an effect on the resale price of the manufacturer's products. Similarly, the manufacturer may impose restrictions on where or to whom a dealer may sell, and these restraints will have highly foreseeable consequences on the price at which a dealer will resell the manufacturer's product. However, they do not constitute vertical price fixing or resale price maintenance, and they are not in and of themselves illegal.

Broadcast Music, Inc. v. Columbia Broadcasting System, Inc., 441 U.S. 1, 23 (1979); *Oreck Corp. v. Whirlpool Corp.*, 563 F.2d 54, 59 (2d Cir. 1977), *cert. denied*, 439 U.S. 946 (1979); *Zenith Radio Corp. v. Matsushita Electric Industrial Co., Ltd.*, 513 F. Supp. 1100, 1146-47 (E.D. Pa. 1981).

TRANSCRIPT OF PROCEEDINGS

Testimony of Gilbert Hartwell

(Witness on Behalf of Defendant)

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HARTWELL — CROSS

* * * *

Q. What made you believe, instead of quitting at that point in time, Mr. Ehrensberger had already been terminated?

A. Because I had already turned down the number 1 machine, which was Cannon.

Q. How many employees did you have at that time when you signed your Sharp dealership, approximately?

A. Approximately six to seven.

Q. All right. Now, at the time that you assumed your Sharp dealership and during the time that you were a Sharp dealer did anyone from Sharp ever tell you that you had to accept and had to price at the suggested list prices that Sharp listed for its various calculators?

A. No.

Q. Did you ever for any reason believe that Sharp was insisting that you price at suggested list price?

A. No.

Q. You testified yesterday, I believe, that hardly a day goes by that you don't make a deal at suggested list price, is that right?

A. We make sales at suggested list price, but we also discount. My sales people have that latitude.

Q. And that happens almost everyday?

A. Yes.

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* * * *

Q. Did you tell him that you would sell your products at the suggested list price if they picked you?

A. No.

Q. Did you tell him that you would sell to the national accounts at the suggested discount and no more, no less if they picked you?

A. No. Wasn't discussed.

Q. What did Mr. Mashos tell you in return in that conversation?

A. Where?

Q. In this conversation you made to him in June 1973 where you ask him to make a choice between either of you?

A. He promised within 30 days he would get back to me.

Q. All right. Now, you testified yesterday that the next time you heard from anybody from Sharp in connection with this was when Mr. Mashos came to advise you in your office in Houston in mid July of 1973. Could you tell us about that meeting and how it occurred, who called whom and what was said at the meeting?

A. Well, his meeting with me at that time was as a result of my call for him to make a decision. So then an appointment was subsequently followed through that he come to Houston to visit with me.

Q. Several weeks later?

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A. Sometime between two to four weeks, almost 30 days, I believe. Maybe it was before 30 days after my call. But it was within the time span.

Q. Now, did he call that meeting to come to consult with you about asking your opinion on whether they ought to cancel Mr. Ehrensberger?

A. No.

Q. What did he tell you?

A. Well, when he came into my office he asked me what were my plans, and so forth, if I was a Sharp dealer. So I told him of what I was prepared to do from crank-up; hire a sales force again, to recruit and start a service department, advertise. And then he subsequently had—well, he immediately told me Mr. Ehrensberger had been notified that he had been terminated, and that Sharp had made the decision for Hartwell's Office World as a their dealer here in Houston.

Q. Did Mr. Mashos ask you anything during that meeting about the prices at which you were going to charge your customers for Sharp products?

A. No. Mr. Mashos' decision had already been made when he arrived in my office in Houston.

Q. Did he ask you anything while he was in your office in mid July 1973 about the pricing policies that you were going to follow?

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A. No.

Q. Did you tell them anything about the pricing policies that you intended to follow?

A. No.

Q. Did you make any commitments to them or discuss at all what your pricing policies had been or would be?

A. No.

Q. Did you come away from that meeting thinking that you had some commitment to Sharp or had made

some commitment; legal, moral or otherwise, to price your products at a particular price?

A. No.

Q. Had you had any prior knowledge before that meeting in mid July 1973 with Mr. Mashos, any prior knowledge at all that Sharp had decided to cancel Mr. Ehrensberger's dealership?

A. Did I know if they had made the decision?

Q. Before that meeting with Mr. Mashos.

A. Yes, sir.

Q. Had you had any information at all that the decision had already been made to cancel Mr. Ehrensberger's dealership?

A. No.

* * * *

Testimony of Thomas George Mashos By Deposition

(Witness on Behalf of Defendant)

[1311]

MASHOS — BY DEPOSITION

Mr. Harvin: Stop on line 20, and pick up on line 27, page 20.

"Q. Was Mr. Ehrensberger's pricing policy something that you kept up with on a regular basis?

"A. No.

"Q. Are the pricing policies of your dealers nationwide something that you kept up with regularly?

"A. Well, we have suggested retail prices, but they sell them for what they want to sell them for.

"Q. Did you terminate Mr. Ehrensberger because he was discounting the product.

"A. Discounting—

"Q. Discounting the product?

"A. No.

"Q. Did you have a policy of terminating discounters?

"A. No.

"Q. Do you know whether there are any other Sharp dealers who engaged in price cutting, price dicounting?

"A. Do I specifically? No.

"Q. Just generally do you know?

"A. Generally I am sure a lot of them do.

"Q. In this lawsuit, Mr. Ehrensberger also alleges that he was terminated pursuant to an agreement between Mr. Hartwell and Sharp to fix the retail price of Sharp calculators in Houston. Did you, Mr. Mashos, have any agreement with Mr.

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Hartwell that he would be required to sell Sharp calculators at a price fixed by Sharp?

"A. No.

"Q. Did you have an agreement with Mr. Hartwell that if Mr. Ehrensberger were terminated, Mr. Hartwell would thereafter sell calculators at prices established by Sharp?

"A. No.

"Q. Mr. Mashos, do you know of any other person at Sharp who might have made such an agreement with Mr. Hartwell that he would sell at prices dictated by Sharp?

"A. No."

Mr. Harvin: Stopping on line 8, page 22.

Go to page 24, line 27.

"Q. When Mr. Hartwell demanded that you terminate Mr. Ehrensberger you didn't refuse to do so, did you?

"A. I did. He requested that many times. Shortly after I became a national sales manager. That was an ongoing complaint by Mr. Hartwell."

Harvin: Stop on line 4. Go down to line 16, page 25.

"Q. Wait. That is not my question. My question is, when he delivered this ultimatum to you you didn't refuse his request, did you? You didn't say to him, 'I'm not going to cancel Mr. Ehrensberger,' did you?

"A. I don't recall saying anything to him except, 'I will have . . .

District Court's Jury Instruction and Special Verdict on Elements for Liability Under Section 1 of the Sherman Act

[1582]

* * * *

The general objectives of the antitrust laws, including the Sherman Act, are to preserve and advance our system of free and open competition, and to secure to everyone an equal opportunity to engage in a business trade and commerce of this country—a policy which is the primary feature of our private enterprise system. The law promotes the concept that free competition yields the best allocation of economic resources, but it also recognizes that in the natural operation of our economic system some competitors are going to lose business while others prosper. Acts become unlawful only when they constitute an unreasonable restraint on interstate commerce.

The specific conduct which Plaintiff claims violated Section 1 of the Sherman Act is an alleged combination, agreement or understanding between Sharp Electronics Corporation and Gilbert Hartwell to terminate Business Electronics as a Sharp dealer because of Business Electronics' price cutting.

Speaking generally, there are three essential elements that the Plaintiff must prove by a preponderance of

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the evidence in order to establish a claim.

(1) That there was an agreement or understanding between Sharp and Hartwell to terminate Business Electronics as a Sharp dealer because of Business Electronics' price cutting;

(2) That the Plaintiff was terminated as a proximate result of the alleged illegal agreement or understanding; and

(3) The amount of money necessary to fairly compensate Plaintiff for the damage proximately caused by Defendant's conduct in violation of the federal antitrust laws.

The burden of proof is on the Plaintiff to establish each one of these elements of his claimed cause of action to your satisfaction by a preponderance of the evidence.

You will be asked to return your verdict in this case in the form of answers to three questions which will be submitted to you concerning the various factual issues in this case. These questions are on the special verdict form that I will now show you. And you will have this in the jury room with you.

At this time I will read this form briefly.

I'm now going to turn to the questions on your special verdict form, and give you the instructions of law

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applicable specifically to your deliberations on each of those questions: of course, as I have told you earlier, you

are to consider all of my instructions as a whole and are not to single out any particular instruction.

Question Number 1 asks you whether you find by a preponderance of the evidence that there was an agreement or understanding between Sharp and Hartwell to terminate Business Electronics as a Sharp dealer because of Business Electronics' price cutting.

An illegal agreement or understanding is formed when two or more persons or corporations knowingly join together to accomplish some unlawful purpose by a concerted action. To act knowingly is to act voluntarily and intentionally, not because of mistake or accident. The essence or an illegal combination, agreement or understanding is an agreement or understanding between two or more persons or corporations to violate or disregard the law. However, the evidence in the case need not show that the members of an alleged illegal combination, agreement or understanding entered into any express or formal agreement.

What a preponderance evidence of the evidence in the case must show in order to establish the existence of the required combination, agreement, or understanding is that Sharp and Hartwell knowingly came to a common and mutual understanding to accomplish or to attempt to accomplish an

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unlawful purpose.

The evidence need not show that the members of the illegal agreement or understanding specifically stated between themselves what their purpose was to be or the

means by which the object or purpose was to be achieved. Purpose or intent may be proved by indirect evidence. While witnesses may see and hear and thus be able to give direct evidence of what each person does or fails to do, there can be no eyewitness account of the state of mind with which the acts were committed. What a person does may indicate either intent or lack of intent.

An illegal combination, agreement or understanding does not need to be in writing. An agreement can be implied where the terms are not declared by the parties but are fairly inferred from the circumstances showing a mutual intention to agree. The term implied agreement refers to a situation where the intention of the parties not manifested by explicit and direct words but is rather by implication or necessary deduction from the circumstances or from the general language or other conduct of the parties.

Plaintiff does not have to show that the persons who joined the alleged illegal combination, agreement or understanding intended to violate the law and knew that they were violating the law. A motivation or intention to

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break the law is not required for there to be an illegal combination, agreement or understanding.

In determining whether Sharp illegally combined or agreed with another party to fix retail prices of calculators, you are instructed that a corporation cannot illegally agree or combine with its officers, employees, or agents. Every act of every officer, employee, or other agent, on behalf of, or in the name of a corporation, if done within

the scope of his authority, is in law the act of the corporation itself. Because a corporation cannot illegally combine or agree with itself, any agreement between officers, employees, or agents of the corporation and the corporation itself cannot constitute an illegal agreement or understanding.

You are instructed Mr. Burkholder was an agent of Sharp, and that Hartwell was not an officer, employee, or agent of Sharp.

It is not necessary for the Plaintiff to join as Defendants in this case all persons who may have participated with the Defendant in the alleged illegal combination, agreement or understanding. A person injured by such an illegal combination, agreement or understanding, if any, may recover against one or all those participating, and he may enforce his right to recover against one, or some, or all, at his election. It is immaterial, as a matter of law,

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that any other member of the alleged combination, agreement or understanding, if any, may have not been joined in this suit by the Plaintiffs.

The Sherman Act is violated when a seller enters into an agreement or understanding with one of its dealers to terminate another dealer because of the other dealer's price cutting. Plaintiff contends that Sharp terminated Business Electronics in furtherance of Hartwell's desire to eliminate Business Electronics as a price-cutting rival.

If you find that there was an agreement between Sharp and Hartwell to terminate Business Electronics because

of Business Electronics' price cutting, you should answer "yes" to Question Number 1.

Sharp, on the other hand, contends that it terminated Business Electronics unilaterally, not as a result of any agreement or understanding with Hartwell, but because of Business Electronics' sales performance. If you find that Sharp did not terminate Business Electronics pursuant to an agreement or understanding with Hartwell to eliminate price cutting by Business Electronics, then you should answer "no" to Question Number 1.

A combination, agreement or understanding to terminate a dealer because of his price cutting unreasonably restrains trade as a matter of law and cannot be justified

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for any reason. Therefore, even though the combination, agreement or understanding may have been formed or engaged in to prevent or halt what the parties perceived to be ruinous price competition or to eliminate any alleged evils of price cutting, it is still unlawful. It makes no difference whether prices were reasonable or unreasonable.

If a dealer demands that a manufacturer terminate a price cutting dealer, and the manufacturer agrees to do so, the agreement is illegal if the manufacturer's purpose is to eliminate the price cutting.

If you answer "yes" to Question Number 1, Question Number 2 asks you to determine whether the alleged combination, agreement, or understanding caused injury to Plaintiff's business. In this connection, Plaintiff contends that the termination of Plaintiff as a Sharp dealer

caused Plaintiff to lose profits from lost sales of electronic calculators.

Plaintiff must establish as a part of its claim that it suffered injury in its business or property as a proximate result of alleged combination or conspiracy. It frequently occurs in the course of normal, lawful competition that some business may suffer economic losses or even go out of business. It is only when such economic losses are caused by unlawful competitive practices that the antitrust laws are violated. An injury to a business can be said to be the

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"proximate result" of antitrust violation only when the act or transaction constituting the violation directly and in natural and continuous sequence produces, or contributes substantially to producing, such injury. In other words, the alleged violation or violations of the Sherman Act by the Defendant, if any, must be a direct, substantial and identifiable cause of the injury which Plaintiff claims to have sustained.

The ultimate success or failure of the combination, agreement or understanding to accomplish the common object or purpose is immaterial, so long as the Plaintiff sustained some damage as a result of the combination, agreement or understanding.

If you find that the alleged combination, agreement or understanding proximally caused injury to Plaintiff's business, then you should answer "yes" to Question Number 2.

* * * *

Supreme Court, U.S.
FILED
AUG 22 1987
JOSEPH F. SPANIOL, JR.
CLERK

NO. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF PETITIONER BUSINESS ELECTRONICS CORPORATION

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DATED: August 21, 1987

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QUESTION PRESENTED

The jury below found an agreement between the defendant supplier and a non-price cutting dealer to terminate a competing dealer for the purpose of eliminating price competition. On appeal, the defendant supplier did not contest the sufficiency of the evidence supporting this finding. Rather, the question presented here is whether dealer termination pursuant to a conspiracy to eliminate price competition constitutes price fixing in violation of the Sherman Act, absent an express finding of direct agreement on resale price levels.

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NO. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF PETITIONER BUSINESS ELECTRONICS CORPORATION*

OPINIONS BELOW

The opinion of the Court of Appeals is reported at 780 F.2d 1212 and appears as Appendix A to the petition for writ of certiorari ("Pet. App."). The district court's unreported ruling denying Sharp Electronics Corporation's motions for a new trial and judgment n.o.v. appears

* Pursuant to Supreme Court Rule 28.1, Business Electronics Corporation has no parent companies, subsidiaries or affiliates.

as Pet. App. B. The *per curiam* opinion denying Business Electronics Corporation's suggestion for rehearing *en banc* appears as Pet. App. C.

JURISDICTION

The judgment of the Court of Appeals was entered on January 21, 1986. A timely Suggestion for Rehearing En Banc was denied on February 20, 1986 (Pet. App. C.). A timely petition for Writ of Certiorari was filed on May 20, 1986. On June 17, 1987, this Court granted the petition. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTE INVOLVED

Section 1 of the Sherman Act, 15 U.S.C. § 1, provides in pertinent part:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal. . . .

STATEMENT OF THE CASE

Nature of the Case.

This case presents a question regarding the scope of the *per se* rule against vertical price fixing under Section 1 of the Sherman Act. Specifically, the question is whether an agreement between a manufacturer and a distributor entered into for the purpose of eliminating price competition from another distributor constitutes a *per se* violation of the antitrust law. The Fifth Circuit below held that *per se* liability requires more than an unadorned agreement to eliminate price competition. According to

the Fifth Circuit, the jury must specifically find that the manufacturer and remaining dealer also agree to set prices "at some level". Since this has never been required as a condition for application of the *per se* rule against price fixing, the Fifth Circuit's erroneous ruling should be reversed.

Factual Background.

From 1968 until July 1973, Business Electronics Corporation ("BEC"), owned and operated by Kelton Ehrensberger, was an authorized dealer in Sharp brand electronic calculators in Houston, Texas.[1] BEC's only business was to buy calculators from Sharp Electronics Corporation ("Sharp") and sell them at retail.

Although Sharp suggested retail prices to its dealers and authorized specific discounts from list prices for certain accounts, BEC frequently sold at lower prices in greater discounts than those authorized by Sharp. Consequently, Sharp's Texas representative, Mr. Burkholder, complained to BEC about this price cutting, noting that BEC was "messing up" the market and "creating dealer complaints." Tr. 73-77, 239-40, 244; Px 52.[2] When BEC encountered problems in obtaining prompt delivery of preferred models in sufficient quantity, Burkholder said that Sharp was in a position to make inventory problems very "painful" for BEC if it continued to price the machines "arbitrarily". Tr. 79-80.

In mid-1972, Sharp threatened cancellation of BEC's dealership. At this time, Hiroshi Kawai, Sharp's vice-

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1. BEC was the sole authorized dealer to Sharp until June 1982.

2. "Tr." refers to the official transcript of the trial record below. "Px" refers to plaintiff's exhibits admitted into evidence below.

president, told Ehrensberger that he should "clean up his pricing structure." Tr. 81. Almost contemporaneously, Sharp appointed an additional dealer in Houston—Hartwell's Office World, owned and operated by Gil Hartwell. Hartwell soon began a campaign to stop BEC's price cutting. Tr. 174-75. In a July 1972 letter to Ehrensberger, copied to Sharp, Hartwell wrote that he would not "compete" with BEC for a particular customer "so the customer won't be able to play one of us against the other in a single 'discount' situation." Tr. 84-85; Px 40. Regarding this letter, Hartwell testified that he "was making the first step to lending some price stability to Mr. Ehrensberger" and that he intended to charge Sharp's suggested list prices. Tr. 276-77. Hartwell further testified that Ehrensberger was discounting from Sharp's suggested list price and that Hartwell wanted to avoid that. Tr. 278.

Hartwell Obtains Sharp's Agreement To Eliminate BEC's Price Cutting.

Hartwell thereafter complained to Sharp, including Burkholder, Tom Mashos (national sales manager) and Kawai, about BEC's price cutting, which Hartwell wanted stopped. Tr. 79, 280, 283, 287, 837. Kawai relayed these complaints to Burkholder and told him to "try to solve the problem." Tr. 628, 629, 636, 639. In October 1972, Burkholder wrote Kawai about "problems created by Ehrensberger," meaning the Hartwell complaints concerning BEC's price cutting. Tr. 933-34. In December 1972, Hartwell wrote to Kawai complaining again about BEC's "price cutting," Px 39; Tr. 88-90, which he wanted Kawai to correct. Tr. 286. Subsequently, Burkholder told Ehrensberger that he wanted BEC "to maintain the correct discount range." Tr. 91.

In mid-1973, Hartwell did more than complain. He demanded that Sharp terminate BEC for the *express* purpose of stopping the discounting. Hartwell delivered an "ultimatum" to Mashos: Because of BEC's price cutting, Hartwell would quit unless Sharp cancelled BEC. Within three weeks, Mashos complied with this demand and terminated BEC. Tr. 189-90, 586, 587, 1355-56. Thereafter, Hartwell remained as Sharp's Houston dealer. Tr. 294.

Hartwell's policy was to sell at Sharp's suggested list prices and he usually adhered to those prices in the years following BEC's termination. Tr. 294-95, 296, 398. Accordingly, Hartwell's gross margin—the difference between his cost of purchasing the product from Sharp and his resale price—increased substantially after BEC was terminated.[3]

The Jury Verdict For BEC.

BEC brought this suit under Section 1 of the Sherman Act, contending that Sharp and Hartwell had conspired to terminate BEC for the purpose of eliminating price competition. The district court submitted the following liability interrogatory to the jury:

> Question 1: Do you find by a preponderance of the evidence that there was an agreement or understanding between Sharp and Hartwell to terminate Business Electronics because of Business Electronics' price cutting?

The court instructed the jury that the plaintiff "must show . . . that Sharp and Hartwell knowingly came to a com-

3. Hartwell's gross profit margins increased from 33% in 1972 and 34% in 1973 to 43% in 1974 and 45% in 1975. Px 119; Tr. 389-91, 1156.

mon and mutual understanding to accomplish or attempt to accomplish an unlawful purpose. . . ." Tr. 1584; Joint Appendix ("JA") 15-16. The court further instructed the jury that:

> Plaintiff contends that Sharp terminated Business Electronics *in furtherance of Hartwell's desire to eliminate Business Electronics as a price cutting rival.* . . . Sharp, on the other hand, contends that it terminated Business Electronics unilaterally, not as a result of any agreement or understanding with Hartwell, but because of Business Electronics' sales performance. If you find that Sharp did not terminate Business Electronics pursuant to an *agreement with Hartwell to eliminate price-cutting* by Business Electronics then you should answer 'No' to Question Number 1.

Tr. 1587, JA 18-19 (emphasis added).

The jury answered Question 1 affirmatively, found that BEC had been injured as a result and awarded $600,000 in damages. Pursuant to 15 U.S.C. § 4, the district court entered judgment for BEC for treble this amount plus attorney fees.

After the district court denied Sharp's motions for judgment n.o.v. and for new trial, Sharp appealed to the United States Court of Appeals for the Fifth Circuit.[4]

4. Sharp did not contest the sufficiency of the evidence supporting the jury's finding of an agreement to terminate BEC for price related reasons. This case accordingly does not present the issue of whether the evidence satisfied the standard for proving collusion set forth in Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984). *See* Section I.C, *infra*. There is also no issue as to the sufficiency of the evidence to support a finding of unlawful price fixing even under the standard articulated by the Fifth Circuit. *See* 780 F.2d at 1219.

The Fifth Circuit's Reversal.

The Fifth Circuit reversed the judgment below and remanded for retrial acknowledging that its holding in this case directly conflicted with the holdings of at least four other circuit courts of appeals. *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 170 (3d Cir. 1979); *Victorian House, Inc. v. Fisher Camuto Corp.*, 769 F.2d 466, 469 (8th Cir. 1985); *Ziddell Exploration, Inc. v. Conval International, Ltd.*, 719 F.2d 1465, 1469 (9th Cir. 1983); and *Bostick Oil Co. v. Michelin Tire Corp.*, 702 F.2d 1207, 1215 (4th Cir.), *cert. denied*, 464 U.S. 894 (1983). The Fifth Circuit elected instead to follow *St. Petersburg Yacht Charters, Inc. v. Morgan Yacht, Inc.*, 457 So.2d 1028, 1050 [1984-1] Trade Cases (CCH) ¶ 65, 985 (Fla. 2d Dist. Ct. App. 1984), interpreting the Florida antitrust act and which is contrary to Supreme Court precedent construing the Sherman Act. *United States v. General Motors Corp.*, 384 U.S. 127, 148 (1966).

SUMMARY OF ARGUMENT

The jury below found that BEC was terminated by an agreement between Sharp and Hartwell in furtherance of Hartwell's desire to be rid of a price cutting rival. Sharp tried, but failed, to convince the jury that its motivation was not the elimination of price competition. JA 18-19. The express purpose of the agreement as found by the jury was to eliminate price cutting, i.e., to eliminate price competition. The Fifth Circuit ruled that the evidence was sufficient to support the jury's verdict. 780 F.2d at 1219. The trier of fact has thus found, on the basis of sufficient evidence, a naked restraint on price competition. Nevertheless, the Fifth Circuit reversed.

The Fifth Circuit's reversal rested entirely on its holding that the jury instructions failed to reflect the proper standard for a *per se* violation of the Sherman Act:

> [W]e hold that, in order for a manufacturer's termination of a distributor to be illegal *per se*, it must be pursuant to a price maintenance agreement with another distributor. That distributor must expressly or impliedly agree to set its price at some level, though not at a specific one. The distributor cannot retain complete freedom to set whatever price it chooses.

780 F.2d at 1218.

Each of these three statements forming the Fifth Circuit's holding is an incorrect statement of the law. A manufacturer's termination of a distributor may be illegal *per se* without being pursuant to a price maintenance agreement with another distributor. *See* Section II, below. Moreover, a *per se* illegal price maintenance agreement does not require a distributor to agree to set its price "at some level". *See* Section I.A, below. Finally, distributors who enter into illegal vertical price fixing agreements with manufacturers always retain "complete freedom" to set whatever prices they choose since such agreements are void and unenforceable as a matter of law. *See Dr. Miles Medical Co. v. John D. Park & Sons,* 220 U.S. 373 (1911) (vertical price fixing restrictions invalid and unenforceable).

In its opinion below, the Fifth Circuit incorrectly interpreted and misapplied the applicable antitrust law to the jury's verdict in this case. The jury's finding that Sharp terminated BEC pursuant to an agreement with

Hartwell to eliminate price cutting by BEC constitutes a *per se* violation of the Sherman Act. This agreement, although vertical in form, did not merely affect price competition indirectly or incidentally: its purpose was the elimination of price competition by BEC and it therefore constitutes a naked restraint on competition in violation of the Sherman Act.

An agreement to eliminate discounting by cutting off supplies to the competing discounter falls squarely within the *per se* ban on price fixing. *See United States v. Parke, Davis & Co.,* 362 U.S. 29 (1960); *United States v. General Motors Corp.,* 384 U.S. 127, 147-48 (1966); *Catalano, Inc. v. Target Sales, Inc.,* 446 U.S. 643 (1980). There is absolutely no principled distinction between a supplier and distributor agreeing to eliminate discounting, which not even Sharp would dispute is *per se* illegal, and agreeing instead to eliminate the discounter. Yet precisely such a distinction is required by the Fifth Circuit's opinion which denies *per se* treatment to the latter agreement. There is also no precedent in the decisions of this Court for requiring a further agreement between the manufacturer and surviving distributor to set prices "at some level". Indeed, this additional requirement clearly contradicts the prior decisions of this Court, *see, e.g., United States v. Parke, Davis & Co.,* 362 U.S. at 43-44, which consistently recognize that an agreement to set prices "at some level" is not necessary for a *per se* illegal vertical price fixing agreement. The Fifth Circuit's unwarranted limitation of the *per se* rule in order to recognize the highly theoretical "freedom" of a surviving distributor to become a price cutter himself defies common sense. No conspiring distributor in the real world will use his freedom to do anything other than raise

his prices or his profit margins, as Hartwell did here. The Fifth Circuit's reasoning is also inconsistent with the rationale of the *per se* rule, which is designed to permit categorical judgments about practices that have proved to be "predominantly" anticompetitive and that almost always "tend" to decrease competition. *Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co.*, 105 S. Ct. 2613, 2617 (1985). An agreement between a manufacturer and distributor to terminate a competitor for the express purpose of eliminating his price competition clearly falls within the class of practices confirmed by experience as predominantly anticompetitive and which will almost always tend to make markets less. rather than more, competitive. *See* Section I.A, below.

Even under the erroneous standard adopted by the Fifth Circuit, the agreement found by the jury between Sharp and Hartwell "to eliminate price cutting by BEC" necessarily implies an understanding between Sharp and Hartwell that Hartwell would not follow the same discounting policy as BEC. This understanding between Hartwell and Sharp arises inescapably from their agreement to eliminate BEC's discounting. *See* Section I.B, below.

The Fifth Circuit's argument for its overly restrictive definition of *per se* illegality in this case also makes no sense when tested against the standard of liability applicable to cases characterized as boycotts. It has long been a *per se* antitrust violation for a manufacturer to combine with one or more distributors to cut off a competing distributor's access to the manufacturer's products for the purpose of eliminating price competition. *See, e.g., United States v. General Motors Corp.*, 384 U.S. 127 (1966); *Spray-Rite Service Corp. v. Monsanto Co.*, 684 F.2d 1226, 1235,

n.4 (7th Cir. 1982), *aff'd on other grounds,* 465 U.S. 752 (1984) (citing cases); ABA Antitrust Civil Jury Instructions (1985 Supp.) Section II.1(4), citing *Monsanto* boycott instruction. No agreement on price, whether direct, indirect or implied, between the manufacturer and the surviving distributor is necessary. *See* Section II, below.

Under any one of the above lines of cases an agreement such as the one found here and uncontested on appeal by Sharp, between a supplier and a non-price cutting dealer to terminate a competing dealer for *the purpose of eliminating price competition,* constitutes a *per se* violation of the Sherman Act. The Fifth Circuit's novel departure from the standard of *per se* illegality for concerted action undertaken for the very purpose of directly eliminating price competition creates a substantial loophole in the prohibition against price fixing, *see* Section III below, is in direct conflict with congressional intent and ignores the fact that any substantial change in the law of vertical price fixing must come from Congress, not from the courts. *See* Section IV, below.

Accordingly, the Fifth Circuit's decision should be reversed and BEC's judgment affirmed.

ARGUMENT

I. An Agreement to Eliminate Price Competition Constitutes Unlawful Price Fixing.

The jury's finding that Sharp terminated BEC pursuant to an agreement with Hartwell to eliminate price cutting by BEC stands condemned as *per se* unlawful because

it constitutes vertical price fixing. As all parties acknowledge, vertical price fixing has been a *per se* violation of the Sherman Act since this Court's decision in 1911 in *Dr. Miles Medical Co. v. John D. Park & Sons,* 220 U.S. 373 (1911). The Court has created an established body of precedent over the intervening seventy-six years condemning all manner of vertical agreements and combinations to limit or eliminate price competition. *See, e.g., United States v. A. Schrader's Sons, Inc.,* 252 U.S. 85 (1920); *Frey & Son, Inc. v. Cudahy Packing Co.,* 256 U.S. 208 (1921); *United States v. Bausch & Lomb Co.,* 321 U.S. 707 (1944); *Schwegmann Bros. v. Calvert Distillers Corp.,* 341 U.S. 384, 386 (1951); *United States v. Parke, Davis & Co.,* 362 U.S. 29 (1960); *Simpson v. Union Oil Co.,* 377 U.S. 13 (1964); *Albrecht v. Herald Co.,* 390 U.S. 146 (1968); *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.,* 455 U.S. 97, 102-03 (1980); and *324 Liquor Corp. v. Duffy,* 107 S. Ct. 720 (1987).

From the earliest years of national antitrust enforcement the Court has strictly adhered to the broadest possible protection of price competition under the Sherman Act, leaving it to Congress to legislate any deviations from that policy.[5] In 1974, Congress made price fixing a felony subject to

5. Congress has three times taken the opportunity to legislate changes in the economic policy of the Sherman Act unqualifiedly condemning vertical price fixing. First by passing the Miller-Tydings amendment to the Sherman Act, 50 Stat. 693 (1937) and then effectively expanding the scope of that amendment with the McGuire amendment to the Federal Trade Commission Act, 66 Stat. 632 (1952). The effect of these amendments was to permit states to legalize certain vertical price fixing agreements. Congress reversed this economic policy in 1975 by repealing the Miller-Tydings and McGuire amendments (effective March 12, 1976) as part of the Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801 (1975).

fines of up to $1 million and up to three years imprisonment. 15 U.S.C. § 1. The Court has repeatedly emphasized the uniquely sensitive role that price competition plays in our economy, thereby making it "an object of special solicitude under the antitrust laws." *General Motors,* 384 U.S. at 148; *see Albrecht v. Herald Co.,* 390 U.S. 145, 154 (1968) (Douglas, J., concurring) (vertical price fixing *per se* illegal because of "great leverage" price has over the market); *United States v. Container Corp. of America,* 393 U.S. 333, 338 (1969) ("Price is too critical, too sensitive a control to allow it to be used even in an informal manner to restrain competition"); *United States v. Socony-Vacuum Oil Co.,* 310 U.S. 150, 226, n.59 (1940) (price is the "central nervous system" of our economy).

Unadorned elimination of price competition is the vice common to all price fixing agreements. *Arizona v. Maricopa County Medical Society,* 457 U.S. 332, 345 (1982) ("The aim and result of every price fixing agreement, if effective, is the elimination of one form of competition.") For this reason the Court has consistently condemned as *per se* illegal all agreements and combinations whose purpose is the direct suppression of price competition, whether the agreements or combinations themselves are termed "horizontal", *see e.g., United States v. Socony-Vacuum Oil,* 310 U.S. 150 (1940); *Arizona v. Maricopa County Medical Society,* 457 U.S. 330 (1982), or vertical, *see e.g., United States v. Parke, Davis & Co.,* 362 U.S. 29 (1960); *Albrecht v. Herald Co.,* 390 U.S. 146 (1968).[6]

6. The Court has often expressed its condemnation of vertical price fixing by referring to the same broad description of price fixing used in horizontal cases. *See, e.g.,* United States v. Parke, Davis

Although the Court has applied the *per se* rule even in horizontal contexts so as not to condemn out of hand *bona fide* joint ventures or other cooperative arrangements when some agreement on price is necessary to market the product at all, *see, e.g., Broadcast Music, Inc. v. Columbia Broadcasting Systems,* 441 U.S. 1, 9, 23 (1979); *NCAA v. Board of Regents,* 104 S. Ct. 2948, 2961 (1984), no such exception is applicable here. BEC's termination was not necessary or incidental to the implementation of some legitimate marketing arrangement between Sharp and its dealers intended to make Sharp products more competitive in the market at large, but rather resulted from Sharp and Hartwell's agreement "in furtherance of Hartwell's desire to eliminate Business Electronics as a price-cutting rival", Tr. 1587, JA-18, and Sharp's purpose to eliminate BEC's price cutting. Tr. 1588, JA-19.

Similarly, the reasons supporting application of the rule of reason to the grant of an exclusive distributorship have no relevance here. The Fifth Circuit mistakenly characterized BEC's termination as similar to an exclusive distributorship, which, though it may have the effect of raising prices, is not illegal *per se*. 780 F.2d at 1216. On the contrary, the evidence here demonstrated, and the

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& Co., 362 U.S. 29, 47 (1960) (condemning vertical price fixing and relying on, *inter alia,* definition of price fixing in *Socony Vacuum Oil*); Simpson v. Union Oil Co., 377 U.S. 13, 18 (1964) (relying upon *Socony Vacuum Oil* and *Parke, Davis*).

Indeed, from its inception the *per se* rule against vertical price fixing has reflected the Court's *per se* condemnation of horizontal price fixing. In the first vertical price fixing decision before the Court, *Dr. Miles,* the Court cited United States v. Addyston Pipe & Steel Co., 175 U.S. 211 (1899), a horizontal price fixing case, in support of its conclusion that the vertical price fixing agreements in question were *per se* violations of the Sherman Act. 220 U.S. at 407-08.

jury found, *more* than a mere exclusive distributorship agreement which might incidentally affect prices. The district court instructed the jury that it could find an unlawful conspiracy *only* if Sharp terminated BEC "pursuant to an agreement . . . with Hartwell *to eliminate price cutting* by BEC. . . ." Tr. 1587, JA-19. Bona fide exclusive distributorship agreements, however, are not aimed at the elimination of a competitor because of his discounting. The punitive termination of one dealer by agreement with a competitor for the purpose of eliminating price competition bears no resemblance, for example, to a network of exclusive distributorships designed by a manufacturer as part of a marketing strategy for the purpose of achieving increased inter-brand competition. *Compare Continental T.V., Inc. v. GTE Sylvania, Inc.,* 433 U.S. 36, 38 (1977) (territorial location restrictions part of manufacturer's marketing strategy to improve market position) *with Com-Tel, Inc. v. DuKane Corp.,* 669 F.2d 404, 411-412 (6th Cir. 1982) ("It would be unrealistic to assert that *DuKane* achieved distribution efficiencies through its arbitrary decision to exclude one customer from access to its products"); *see* L. Sullivan, Handbook of the Law of Antitrust (1977) ("Sullivan") 429 (citing cases). The agreement found by the jury below had nothing to do with rendering Sharp more competitive in the market at large and everything to do with the suppression of price competition.

A. An Agreement to Set Prices "At Some Level" Is Not Required for a *Per Se* Price Fixing Violation.

Because of the uniquely privileged position price competition enjoys under the antitrust laws, this Court has

consistently condemned vertical and horizontal price fixing in the broadest possible terms. *See United States v. Parke, Davis & Co.*, 362 U.S. at 47 ("any combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal *per se*", quoting *United States v. Socony Vacuum Oil Co.*, 310 U.S. at 223); *Socony Vacuum Oil Co.*, 310 U.S. at 222 (offense of price fixing does not require that prices be "fixed in the sense that they were uniform and inflexible. Price-fixing has no such limited meaning.").

Combinations and conspiracies to suppress or eliminate price competition have been declared *per se* illegal for decades without any requirement that the participants agree to set prices "at some level". *See, e.g., Sugar Institute v. United States*, 297 U.S. 553 (1936) (agreement to adhere to previously announced prices and terms of sale held *per se* unlawful even though the particular prices and terms were not themselves fixed by agreement); *United States v. Socony Vacuum Oil Co.*, 310 U.S. 150 (1940) (concerted program of buying surplus gasoline on the spot market in order to prevent falling prices held *per se* unlawful despite no direct agreement on actual prices); *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980) (agreement to fix trade credit held *per se* unlawful even absent direct agreement on prices); *United States v. Gasoline Retailers Association*, 285 F.2d 688 (7th Cir. 1961) (agreement not to advertise prices is *per se* illegal price fixing even without direct agreement on price); *United States v. United Liquors Corp.*, 149 F.Supp. 609 (W.D. Tenn. 1956), *aff'd per curiam*, 352 U.S. 991 (1957) (agreements establishing uniform costs and markups, adopting classifications of customers entitled to discounts and the percentage of

functional discounts held *per se* unlawful even though there was no agreement as to the price level from which individual dealers would compute discounts); *United States v. American Smelting & Ref. Co.*, 182 F.Supp. 834 (S.D.N.Y. 1960) (agreement specifying price differentials between grades of product held *per se* unlawful); *and see National Society of Professional Engineers v. United States*, 435 U.S. 679 (1978) (engineering society's canons of ethics prohibiting professional engineers from discussing prices with potential customers held unlawful on their face).

Indeed, in vertical price fixing cases it is well settled that "agreements" to set prices—whether express or implied—are not required for *per se* violations of the Sherman Act. *See, e.g., United States v. Parke, Davis & Co.*, 362 U.S. 29, 43-44 (1960) (price maintenance agreement, express or implied, not necessary for unlawful combination: "The Sherman Act forbids combinations of traders to suppress competition"); *United States v. General Motors Corp.*, 384 U.S. at 147-48 (concerted elimination of sales to discounters held *per se* unlawful even though only indirectly affecting price); *see also United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707, 722 (1944) ("The Beech-Nut Company, without agreements, was found to suppress the freedom of competition by coercion of its customers through special agents of the company, by reports of competitors about customers who violated resale prices, and by boycotts of price cutters.). In *Parke, Davis* the Court struck down as *per se* unlawful price fixing an illegal combination among a supplier (Parke, Davis), its wholesalers and its retailers to cut off supplies of Parke, Davis products to discounting retailers without finding any agreement.

In *Catalano, Inc. v. Target Sales, Inc.*, this Court held that an agreement to eliminate credit terms was "tantamount to an agreement to eliminate discounting, and thus [fell] squarely within the traditional *per se* rule against price fixing." 446 U.S. at 648. The Court noted that:

> in . . . *Socony Vacuum* . . . we held that a program of buying surplus gasoline on the spot market in order to prevent prices from falling sharply was unlawful without any inquiry into the reasonableness of the program, *even though there was no direct agreement on the actual prices to be maintained.* . . .
>
> Thus we have held agreements to be unlawful *per se* that had substantially less direct impact on price than the agreement alleged in this case.

Id. at 647 (emphasis added). The Court further noted that the agreement to eliminate discounting was "merely one form of price fixing." *Id.* at 650.

There is thus no question that if BEC had agreed with Sharp (or with Hartwell) to eliminate its discounting there would have resulted a *per se* violation of the Sherman Act for price fixing. *United States v. Parke, Davis & Co., supra; Catalano, Inc. v. Target Sales, Inc., supra.* The record below demonstrates that Sharp and Hartwell tried to get BEC's cooperation in just such an agreement. Tr. 73-77, 79-81, 84-85, 74-75, 239-40, 276-77. After BEC refused, Sharp and Hartwell agreed to eliminate BEC's discounting themselves by the simple expedient of eliminating the discounter, BEC. In *General Motors,* the Court recognized that this constitutes a distinction without a difference for purposes of applying the *per se* rule.

The Court refused "to construe the Sherman Act to prohibit conspiracies to fix prices at which competitors may sell, but to allow conspiracies or combinations to put competitors out of business entirely." 384 U.S. at 148. The jury below found that BEC was put out of business entirely by an agreement between Sharp and Hartwell to eliminate BEC's price cutting. JA 18-19. This concerted action by Sharp and Hartwell for the purpose of eliminating price competition by BEC clearly warrants application of the *per se* rule against vertical price fixing. *United States v. General Motors, supra; United States v. Parke, Davis & Co., supra; Catalano, Inc. v. Target Sales, Inc., supra.*

The Fifth Circuit ignored or rejected these precedents and reasoned that an agreement to terminate a price cutter does not literally "fix" prices at any specific or general level but "merely frees the complaining dealer to set prices he chooses." 780 F.2d at 1216. The Fifth Circuit's reasoning can only be understood as a concern to recognize the theoretical "freedom" of the conspiring dealer to become a price cutter himself, thereby making application of the *per se* rule inappropriate. Under comparable reasoning, a bank robber is also theoretically "free" to return stolen money to the bank, but even a little experience in the world at large teaches that such freedom is not likely to be exercised. As a matter of common sense, no dealer who agrees with a supplier to terminate a competitor in order to eliminate that competitor's price cutting will do anything other than raise his prices or his profit margins following the termination. In fact, that is precisely what happened in this case. Hartwell's gross profit margins rose substantially (from 33% in 1972 and 34% in 1973 to 43% in 1974 and 45% in 1975) following BEC's termination. Px 119, Tr. 389-91, 1156.

The misguided notion that elimination of a price cutting competitor merely "frees" the remaining dealer to engage in discounting overlooks entirely the very purpose of the concerted termination and completely ignores the practical realities of this case and cases like it.

Limiting the *per se* rule because of the extremely unlikely possibility that a successfully conspiring dealer might then turn around and begin price cutting himself misunderstands the proper role of the *per se* rule. The *per se* rule is designed to permit economical, categorical judgments with respect to business practices that have proved to be "predominantly" anticompetitive, that almost always "tend" to decrease economic efficiency and render markets less, rather than more, competitive. *See Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co.*, 105 S. Ct. at 2617; *National Collegiate Athletic Ass'n v. Board of Regents of University of Oklahoma*, 104 S. Ct. 2948, 2962 (1984) (*per se* rules apply when surrounding circumstances make the "likelihood" of anticompetive conduct so great as to render unjustified further examination of challenged conduct). Thus, even when, under an unusual set of circumstances, the *per se* rule invalidates some agreements that a full inquiry might have proved reasonable, this result is tolerated for the sake of business certainty and litigation efficiency. *Arizona v. Maricopa County Medical Society*, 457 U.S. 330, 343-44 (1982). *Per se* rules are designed to be "broad generalizations" about the social utility of particular practices, *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 50, n.16, and must therefore be based on common experience rather than uncommon and highly theoretical exceptions:

> Cases that do not fit the generalization may arise, but a *per se* rule reflects the judgment that such cases are not sufficiently common or important to justify the time necessary to identify them.

Id.

In the present case, common sense and experience teach that conspiring dealers who use their theoretical "freedom" to become discounters will be neither "sufficiently common or important to justify the time necessary to identify them" and do not, therefore, warrant a limitation on the *per se* rule such as the Fifth Circuit has imposed.

B. The Agreement to Eliminate BEC's Price Cutting Necessarily Implies an Agreement Between Sharp and Hartwell to Set Prices "At Some Level".

Although as discussed above, the *per se* rule against price fixing has never required violators to agree to set prices "at some level", the agreement found by the jury in this case necessarily implies such an agreement between Sharp and Hartwell. The jury's finding that Sharp agreed with Hartwell to terminate BEC *in order to eliminate BEC's price cutting* entails an understanding between Sharp and Hartwell that Hartwell would not pursue the BEC's same discounting policy. In other words, the jury's finding requires the conclusion that Sharp and Hartwell agreed to set prices at a level higher than BEC's, "though not a specific one." 780 F.2d at 1218. No other interpretation of the Sharp-Hartwell agreement makes any economic sense. *Cf. Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 106 S. Ct. 1348, 1361-62 (1986) (absense of any rational motive to conspire excludes jury inference of conspiracy). Vertical price fixing agreements

"implied from a course of dealing or other circumstances" are just as subject to the rule of *per se* illegality as express agreements. *United States v. A. Schrader's Son, Inc.*, 252 U.S. 85 (1920); *Frey & Son, Inc. v. Cudahy Packing Co.*, 256 U.S. 208, 210 (1921) (essential agreement, combination or conspiracy may be implied from a course of dealing or other circumstances); *see also United States v. Parke, Davis & Co.*, 362 U.S. 29, 43-44 (combinations of traders to suppress competition are sufficient to trigger Sherman Act liability, neither express nor implied agreements are required).

Accordingly, since the jury's verdict in this case necessarily implies an agreement that Hartwell would not follow the discounting policies of the distributor he and Sharp had just agreed to terminate precisely in order to eliminate such discounting, even the erroneous standard of liability articulated by the Fifth Circuit was satisfied here.

C. Monsanto Does Not Justify Naked Restraints On Price Competition.

Although acknowledging that *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), "did not expressly disapprove" the rule embodied in the jury instructions below, 780 F.2d at 1218, the Fifth Circuit nevertheless extrapolated the *Monsanto* holding beyond its intended limit. In *Monsanto*, this Court held that concert of action cannot be inferred from mere evidence of dealer pricing complaints followed by termination in response to those complaints. The Court found such evidence to be "highly ambiguous," since it does not exclude the possibility that the manufacturer unilaterally decided to terminate. Thus, *Monsanto* requires the plaintiff to adduce additional "evidence that tends to exclude the

possibility that the manufacturer and non-terminated distributor were acting independently." 465 U.S. at 764. Going far beyond this holding, the Fifth Circuit concluded that even an actual *agreement* to terminate because of price cutting does not constitute price fixing, since, the court reasoned, only a "mind reader" could distinguish between such an agreement and unilateral termination in response to dealer complaints. 780 F.2d at 1218. The Fifth Circuit's reasoning will not withstand analysis.

First, *Monsanto* dealt only with the minimum proof required to show concert of action. Here, Sharp did not contest the sufficiency of evidence supporting the jury finding of collusion. Second, asking the trier of fact to determine whether the evidence shows an agreement to terminate for the purpose of eliminating price cutting entails no extraordinary feat. Every day juries are asked to find the presence (or absence) of specific intent, based upon direct and circumstantial evidence. Here, the evidence supporting the jury's finding of intent was overwhelming and required no mind-reading skills, only the ability to draw reasonable inferences. The Fifth Circuit itself observed:

> There was evidence that, even before Hartwell became a dealer, Sharp sought BEC's adherence to the suggested retail price list. BEC produced evidence tending to show that it was not "free-riding" and that its sales performance was equal to Hartwell's. The logical inferences from such evidence, if drawn by the jury, could support a finding that BEC's termination was not due to the reasons Sharp suggests.
>
> In addition, there was evidence that Hartwell usually followed Sharp's suggested prices. There was also evidence that Hartwell sought to encourage BEC to fol-

> low these prices. Finally, the record shows that Hartwell complained vigorously to Sharp about BEC's pricing and that ultimately Sharp responded by terminating BEC. This evidence, taken as a whole and viewed in the light most favorable to BEC, could support an inference that Sharp and Hartwell had agreed that Hartwell would follow Sharp's suggested retail prices and that BEC's termination was pursuant to this agreement.

780 F.2d at 1219 (citation omitted). This evidence, along with Hartwell's express demand that Sharp terminate BEC for price cutting, satisfies the *Monsanto* requirement of "evidence which tends to exclude the possibility that the manufacturer and non-terminated distributor were acting independently," and removes this case from the mere "termination-in-response-to-complaints" category.

II. Whether Strictly Characterized as Price Fixing or Not, an Agreement Between Manufacturer and Dealer to Terminate a Discounting Competitor for the Purpose of Eliminating Price Competition is Illegal *Per Se*.

An agreement between a manufacturer and one or more distributors to cut off a competing distributor's access to the manufacturer's products for the purpose of eliminating price competition has been condemned as a *per se* illegal in virtually every circuit to consider the issue. *See, e.g., Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979); *Malley-Duff & Associates v. Crown Life Ins. Co.*, 734 F.2d 133 (3d Cir.), *cert. denied*, 469 U.S. 1072 (1984); *Bostick Oil Co. v. Michelin Tire Corp.*, 702 F.2d 1207 (4th Cir.), *cert. denied*, 464 U.S. 894 (1983); *Jayco Systems v. Savin Business Machines Corp.*, 777 F.2d 306, 317-18 (5th Cir. 1985) (*per se* violation

where supplier refuses to deal with or acts to terminate a customer at the behest of the customer's competitor); *Com-Tel, Inc. v. Dukane Corp.*, 669 F.2d 404 (6th Cir. 1982); *Spray-Rite Service Corp. v. Monsanto Co.*, 684 F.2d 1226, 1235 n.4 (7th Cir. 1982), *aff'd on other grounds*, 465 U.S. 752 (1984) (Monsanto could not lawfully terminate Spray-Rite's distributorship pursuant to an agreement with its distributors because such conduct is a concerted refusal to deal which is *per se* unlawful even if not part of a scheme to fix resale prices); *Victorian House, Inc. v. Fisher Camuto Corp.*, 769 F.2d 466 (8th Cir. 1985); *Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc.*, Slip Op., LEXIS Gen. Fed. Library (8th Cir. 1987); *Ziddell Exploration, Inc. v. Conval International, Ltd.*, 719 F.2d 1465, 1469 (9th Cir. 1983); *see also M & H Tire Co. v. Hoosier Racing Tire Corp.*, 733 F.2d 973 (1st Cir. 1984).[7]

Many of these decisions rely not only upon traditional price fixing analysis, but also upon a group boycott

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7. Only some decisions in the Fifth, Seventh and Tenth Circuits appear to have taken the position that a concerted refusal to deal in order to suppress price competition is not *per se* illegal. *See, e.g.*, Business Electronics Corp. v. Sharp Electronics Corp., 780 F.2d 1212 (5th Cir. 1986); Morrison v. Murray Biscuit Co., 797 F.2d 1430, 1440 (7th Cir. 1986) (Posner, J.) (following *Sharp*); Westman Com'n Co. v. Hobart Intrn., Inc., 796 F.2d 1216, 1223 (10th Cir. 1986) (following *Sharp*).

The Tenth Circuit's adherence to *Sharp* may be more in form than in substance. *Westman* did not involve the termination of a price-cutting distributor but rather a manufacturer's refusal to appoint plaintiff as a new distributor at the urging of an existing distributor who feared the prospect of new competition. 796 F.2d at 1219. Thus, unlike the case at bar, no actual competition was extinguished in *Westman*, see Sullivan, 428-29, and there was no indication that the plaintiff was a price-cutter or that the refusal to deal was intended to have any direct effect on price. *Compare* 796 F.2d at 1223.

analysis. In *Monsanto,* for example, the trial court instructed the jury in both price fixing and boycotts as alternative theories of liability, *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. at 758, n.2 (interrogatories 1 and 3), and the court of appeals affirmed the boycott instruction, *Spray-Rite Service Corp. v. Monsanto,* 684 F.2d at 1235, n.4. The *Monsanto* boycott instruction is part of the ABA's Antitrust Civil Jury Instructions (1985 Supp.) § II.A.(4) "Refusal to Deal". *And see Jayco Systems v. Savin Business Machines Corp.*, 777 F.2d at 318, n.41 (facts that might justify a preliminary finding of group boycott would be where supplier, alone or with other dealers, conspired with complaining dealer to deny supplies to a competitor). With respect to the kind of agreement at issue here, these alternative theories of *per se* liability—price fixing or group boycott—complement each other. An agreement to terminate a discounter in order to eliminate his discounting is a concerted refusal to deal whose purpose is to eliminate price competition by a competitor.[8]

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8. As a practical matter there can be no bright line drawn between vertical price fixing to eliminate discounts and group boycotts to eliminate discounters. In *General Motors,* for example, which is traditionally treated as a boycott case, Justice Harlan concurred by noting that there was no tenable reason for differentiating it from the Court's vertical price fixing decision in United States v. Parke, Davis & Co., 362 U.S. 29 (1960) and concluded that *Parke, Davis* controlled. 384 U.S. at 148-149. Cernuto, Inc. v. United Cabinet Corporation, 595 F.2d 164 (3d Cir. 1979), which relied on the boycott case of *General Motors,* was a resale price maintenance case. *Cernuto,* however, is frequently cited as precedent in boycott cases. *See, e.g.,* Malley-Duff & Associates v. Crown Life Ins. Co., 734 F.2d 133 (3d Cir.), *cert. denied,* 469 U.S. 1072 (1984); Victorian House, Inc. v. Fisher Camuto Corp., 769 F.2d 466 (8th Cir. 1985). Whether characterized as "price fixing" or "boycott", the conduct has the purpose of eliminating competition—a naked restraint of trade under the Sherman Act.

The Fifth Circuit's argument for its overly restrictive definition of *per se* illegality makes no sense when tested against the standard of liability applicable to cases characterized as illegal boycotts.[9] Under the Fifth Circuit's rule, the same behavior calls for application of the rule of reason if it is called vertical price fixing and the *per se* rule if it is called a boycott.

A seminal group boycott case, *Klor's Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959), supports application of the *per se* rule here. In *Klor's,* Broadway-Hale, a department store competitor of plaintiff Klor's, allegedly combined with ten national manufacturers and their distributors to cut off supplies to Klor's or to sell to Klor's only at highly unfavorable terms. 359 U.S. at 208-209. This Court found the resulting group boycott to constitute a *per se* violation of the Sherman Act. Although Klor's sold a wide variety of retail appliances, the "wide combination consisting of manufacturers, distributors and a retailer" eliminated Klor's "freedom to buy appliances in an open competitive market" and deprived the manufacturers and their distributors of the freedom to sell to Klor's. 359 U.S. at 213. The Court rejected any analogy

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9. The Court has aptly noted that boycotts "are not a unitary phenomenon". Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co., 105 S. Ct. at 2619, *quoting* St. Paul Fire & Marine Ins. Co. v. Barry, 438 U.S. 531, 543 (1978). The Court has generally applied the *per se* approach to

> joint efforts *by a firm* or firms to disadvantage competitors by either directly denying or persuading or coercing suppliers or customers to deny relationships the competitors need in the competitive struggle.

105 S. Ct. at 2619, *quoting* Sullivan, 261-262 (emphasis added). *And see* Sullivan, 231, n.1.

There is even greater reason to condemn a concerted refusal to deal such as the one here whose express purpose is to extinguish price competition. *See* United States v. General Motors Corp., 384 U.S. at 148.

between the combination instigated by Broadway-Hale, whose purpose and effect was to eliminate Klor's as an effective competitor, and the unilateral refusal to deal by one trader with another or a manufacturer and a dealer agreeing to an exclusive distributorship. 359 U.S. at 212. A contrary rule would mean that "a group of powerful businessmen may act in concert to deprive a single merchant, like Klor, of the goods he needs to compete effectively." 359 U.S. at 210.

Similarly, *United States v. General Motors Corp.*, 384 U.S. 127 (1966), strongly supports application of the *per se* rule to the instant case. In *General Motors* a number of Chevrolet dealers in the Los Angeles area supplied discount houses with new Chevrolets which were in turn sold to consumers at allegedly bargain prices. 384 U.S. at 130-132. As the volume of these discount sales increased, Chevrolet dealers located near the discount outlets began to feel the pinch. Members of the local Chevrolet Dealers Association attempted to persuade Chevrolet dealers doing a substantial business with the discounters to stop, but to no avail. 384 U.S. at 133-34. Finally, the dealers enlisted the agreement of their common supplier General Motors, to put a stop to the sales to discounters. Within a month, General Motors had elicited from each dealer a promise not to do business with the discounters. 384 U.S. at 136.

In *General Motors* this Court held that the acts just described constituted "a classic conspiracy in restraint of trade: joint collaborative action by dealers, the appellee associations, and General Motors to eliminate a class of competitors by terminating business dealings between them and a minority of Chevrolet dealers. . . ." 384 U.S. at 140. The Court summarily rejected General Motors'

argument that its actions should be judged by the rule of reason as applied to its dealer location clause,[10] rejected the finding of the district court that the actions of the defendants were "unilateral" or "merely parallel" as being beyond any "stretch of the imagination" and declared that

> Elimination by joint collaborative action of discounters from access to the market is a *per se* violation of the Act.

384 U.S. at 145. The Court cited *Klor's* and other boycott cases in support of its decision:

> The principle of these cases is that where businessmen concert their actions in order to deprive others of access to merchandise which the latter wish to sell to the public, we need not inquire into the economic motivation underlying their conduct. . . . Exclusion of traders from the market by means of

10. *General Motors* apparently tried to argue that its actions should be judged under the rule of reason enunciated in White Motor Co. v. United States, 372 U.S. 253 (1963) since the same results could just as well have been obtained by General Motors' unilateral enforcement of its dealer location clause. The Court summarily rejected this attempt to justify what *General Motors* actually did (reaching agreement with dealers to eliminate sales to discounters) by what it might have done (unilaterally enforce its dealer location clause). Having unlawfully combined with its dealers,

> [W]hatever *General Motors* might or might not lawfully have done to enforce individual Dealer Selling Agreements by action within the borders of those agreements and the relationship which each defines, is beside the point.

384 U.S. at 140. The fact that there may also be lawful means to achieve the same or substantially similar results achieved by illegal means obviously cannot immunize unlawful behavior. In the instant case, for example, the fact that Sharp might have lawfully terminated BEC unilaterally under United States v. Colgate Co., 250 U.S. 300 (1919), does not immunize Sharp from liability when it combined all BEC's competitors to do so.

> combination or conspiracy is so inconsistent with the free-market principles embodied in the Sherman Act that it is not to be saved by reference to the need for preserving the collaborators' profit margins or their system for distributing automobiles. . . .

384 U.S. at 146.

The Court went on to note yet another reason for condemning the combination in *General Motors* as illegal ***per se***:

> [I]nherent in the success of the combination in this case was a substantial restraint upon price competition—a goal unlawful *per se* when sought to be effected by a combination or conspiracy; *e.g., United States v. Parke, Davis & Co.,* 362 U.S. 29; *United States v. Socony-Vacuum Oil Co.,* 310 U.S. 150. And the *per se* rule applies even when the effect upon prices is indirect. *Simpson v. Union Oil Co.,* 377 U.S. 13; *Socony-Vacuum Oil Co., supra.*
>
> There is in the record ample evidence that one of the purposes behind the concerted effort to eliminate sales of new Chevrolet cars by discounters was to protect franchise dealers from real or apparent price competition. . . .
>
> The protection of price competition from conspiratorial restraint is an object of special solicitude under the antitrust laws. We cannot respect that solicitude by closing our eyes to the effect upon price competition of the removal from the market by a combination or market, by a combination or conspiracy, of a class of traders. Nor do we propose to construe the Sherman Act to prohibit conspiracies to fix prices at which competitors may sell, but to allow conspiracies or combinations to put competitors out of business entirely.

384 U.S. at 147-48.

The principles used by the Court to condemn the anticompetitive combinations in *Klor's* and *General Motors* are equally applicable to the present case. Hartwell, BEC's competitor, first sought BEC's cooperation in terminating its discounting of Sharp products. When that effort failed, Hartwell, like Broadway-Hale and the General Motors dealers, used its leverage with their common supplier to obtain an agreement to cut off BEC's supplies. As was the case in *General Motors,* Hartwell needed only to reach agreement with one supplier, Sharp, because Sharp was BEC's sole source of supply: BEC sold no other products. What Hartwell was therefore powerless to achieve alone, he was able to achieve by agreement with Sharp. The result, as in *General Motors,* is a "classic conspiracy" to drive out competition. 384 U.S. at 140.

This is accordingly *not* a case in which firms engage in some legitimate joint effort seemingly "designed to increase economic efficiency and render markets more, rather than less competitive." *See, e.g., Northwest Wholesale Stationers, Inc.,* 105 S. Ct. at 2620 (reasonable rules necessary for functioning of wholesale purchasing cooperative enabling smaller retailers to compete more effectively judged by "rule of reason" standard). The joint effort between Sharp and Hartwell here was simply a conspiracy to eliminate price competition by BEC, not to render Sharp more competitive in the market at large. *Id.,* (practices subject to *per se* rule "were generally not justified by plausible arguments that they were intended to enhance overall efficiency and make markets more competitive."). The jury found that Sharp and Hartwell agreed to eliminate BEC *because* of its price cutting. This "vertical" agreement represents the

elimination of price competition by one competitor at the instigation of another. As Professor Sullivan has noted:

> when an existing dealer enlists the manufacturer to choke off one of the dealer's competitors, although the 'agreement' which enables Section 1 to be invoked is vertical, the restraint thereby achieved is horizontal in its impact: *it is an attack by one dealer against another.*

Sullivan, 429 (emphasis added).

The present case warrants *per se* condemnation of the Hartwell-Sharp agreement to eliminate BEC's price cutting on the same principles applied to illegal boycott to drive out competition in *General Motors* and *Klor's.*

Some courts appear to reject direct application of "classic" boycott rules unless there is some element of horizontal collusion present. *See, e.g., Lomar Wholesale Grocery, supra,* Slip Op. at 15 ff. (refusals to deal involving no concerted action between horizontal competitors do not constitute unlawful group boycotts) (citing cases). Other courts have taken a different view. *See, e.g., Com-Tel v. DuKane Corp.,* 669 F.2d 404 (6th Cir. 1982); *M & H Tire Co. v. Hoosier Racing Tire Corp.,* 733 F.2d 973, 978 (1st Cir. 1984).

Clearly, however, the principles condemning anticompetitive boycotts *per se* do not require horizontal collusion at the "blockaded" or dealer level, since *Klor's* involved the action of only one firm at that competitive level, Broadway-Hale. Just as clearly, horizontal collusion need not be present at the "blockading" or supplier level, since *General Motors* concerned the action of only one firm at that competitive level, General Motors Corporation. In fact, the presence of horizontal collusion in both these cases was only incidental to the effective exercise of vertical leverage against the targeted dealer. In *General Motors,* for example, although non-discounting Chevrolet dealers were part of the unlawful conspiracy, their "horizontal" collusion had been utterly ineffective in halting sales to discounters. 384 U.S. at 133-34. Only the dealers' success in enlisting General Motors to agree to exploit its vertical leverage as the sole source of supply of Chevrolet automobiles to Chevrolet dealers rendered the boycott in *General Motors* effective. Similarly, in *Klor's* the only horizontal collusion in that case took place at the supplier level. The agreement among major appliance manufacturers not to deal with Klor's or to deal only on unfavorable terms made the boycott in that case effective, since Klor's carried a full line of appliances from a variety of manufacturers without substantially all of *Klor's* suppliers enlisted as part of the boycott, *Klor's* would otherwise have been able to continue competing with Broadway-Hale. The essential conditions of a successful boycott were met in *Klor's* by each manufacturer agreeing with Broadway-Hale to discriminate against Klor's, not by allegedly agreeing with each other to do so. Where, as in the present case, a dealer has only a single source of supply, of course, no collusion at the supplier level is required to make the boycott effective.

As Professor Sullivan observed in his discussion of the *per se* rule applied to boycotts:

> [I]t is conceivable that only a single firm at the blockaded level [Hartwell] may succeed in coercing or inducing . . . one important supplier [Sharp] from dealing with one or more would-be competitors

> [BEC] . . . such an arrangement would display all essential elements of a boycott.

Sullivan 231, n.1.

In the present case, just as in the cases of *Klor's* and *General Motors,* the harmful effects on the victims of the boycotts — BEC, Klor's and the discounting Chevrolet dealers—do not depend upon the existence of any horizontal collusion but rather upon the anticompetitive agreements between the competing dealer and common supplier in which the supplier's leverage is exploited to choke off competition at the dealer level. It is the vertical leverage of the target company's supplier, exerted in concert with the target's competitor, that constitutes the boycott. Such concerted action taken for the purpose of excluding a competitor from the market warrants application of the *per se* rule whether or not there is any horizontal collusion. *See General Motors,* 384 U.S. at 146 ("The principle of these cases is that where businessmen concert their actions in order to deprive others of access to merchandise which the latter wish to sell to the public, we need not inquire into the economic motivation underlying their conduct."); *Com-Tel, Inc.,* 669 F.2d at 414 ("The application of group boycott theory does not turn on the number of parties in a combination; rather it is applied to prohibit the exclusionary practices inherent in a boycott which are inconsistent with the free-market principles embodied in the Sherman Act").

Even courts which resist applying the boycott rules directly without some horizontal collusion being present make an exception for and include within the *per se* rule vertical concerted refusals to deal which are "price related" as in the case at bar. *See, e.g., Lomar Wholesale Grocery,*

Slip Op. at 15-16 (vertical concerted refusals to deal subject to rule of reason analysis unless price-related or designed to enforce underlying restrictions otherwise subject to *per se* analysis).

Per se treatment is especially warranted where, as here, the challenged agreement expressly seeks to restrain price competition, "an object of special solicitude under the antitrust laws." *General Motors,* 384 U.S. at 148. To reject the application of the *per se* rule to an agreement whose purpose is so explicitly anticompetitive would require this Court to "[close its] eyes to the effect of price competition of the removal from the market by combination of conspiracy" of the only source of intra-brand competition for Sharp products in the Houston market. *Id.* The Court has previously rejected proposals "to construe the Sherman Act to prohibit conspiracies to fix prices at which competitors may sell, but to allow conspiracies or combinations to put competitors out of business entirely." *Id.* The Court has thus squarely condemned as unlawful *per se* agreements such as the one at issue here to terminate a rival for price cutting.

III. The Fifth Circuit's Decision Creates an Unprecedented, Substantial Loophole in the Important Federal Prohibition Against Price Fixing.

The Fifth Circuit's decision creates an enormous "loophole" in the important federal prohibition against price fixing. The Fifth Circuit's ruling permits a dealer to use a manufacturer as his agent in order to eliminate a competitor who refuses to fix prices. Dealers may therefore obtain a manufacturer's agreement to police discounting by other dealers so long as the manufacturer and dealer

do not agree "on some price level." The result is a trivialization of the *per se* rule against vertical price fixing. For manufacturers and distributors interested in eliminating discounting, there is simply no need for an agreement on specific prices if the *per se* rule can be evaded simply by agreeing to terminate any discounters. The Fifth Circuit's decision would substantially rob the *per se* rule against vertical price fixing of most practical application, particularly with respect to price restraints initiated by dealers, which typically present the greatest danger to competition.[11]

IV. Congress Has Rejected The Limitation On The *Per Se* Rule Put Forward In The Decision Below And Any Substantial Change In The Law Of Vertical Price Fixing Must Come From Congress.

As demonstrated above, a naked agreement between a manufacturer and distributor for the purpose of eliminating price competition from a competitor has long been condemned as *per se* illegal under the Sherman Act. Since passage of the Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801, Congress has repeatedly endorsed an unqualified *per se* rule against vertical price fixing. *See Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 51, n.18 (1977) (Noting that Congress recently expressed approval of a *per se* analysis of vertical price restrictions by enacting Consumer Goods Pricing Act of 1975). Congress has opposed not

11. The question of whether vertical price fixing should continue to be *per se* illegal as it has since 1911 is raised by Sharp's cross-petition, upon which the Court has not yet acted. Accordingly, petitioner BEC has not addressed this issue.

only the obvious overruling of the *per se* rule but also any attempt to dilute or trivialize it.

On January 23, 1985, the Department of Justice published its Vertical Restraints Guidelines, *reprinted in* 5 [Trade Reg. Rep.] (CCH) ¶ 50,473. In an effort to urge a greatly reduced *per se* rule applicable to vertical price fixing, the Guidelines proposed a qualification of the rule similar to that adopted by the Fifth Circuit below:

> Before characterizing a practice as a price restraint subject to *per se* condemnation, there must be an agreement between a supplier and its distributors as to resale prices. . . .
>
> The Guidelines will apply *unless* there is direct or circumstantial evidence (other than effects on price) establishing an *explicit agreement as to the specific prices at which the goods or services would be resold.*

Id. at p. 56,191 (emphasis added).

Congress reacted by denouncing the Guidelines as an inaccurate statement of case law and of congressional intent:

> Whereas such policy guidelines are inconsistent with established antitrust law as reflected in Supreme Court decisions and statements of congressional intent . . . in stating that *vertical restraints that have an impact upon prices are subject to the per se rule of illegality only if there is an "explicit agreement as to specific prices";* in stating that restraints imposed by a manufacturer at the request of dealers are vertical in nature and therefore not subject to the *per se* rule of illegality. . . . Now, therefore, be it

> Resolved, That it is the sense of the Congress that the antitrust enforcement policy guidelines stated in "Vertical Restraints Guidelines", published by the Department of Justice on January 23, 1985—
>
> (1) *are not an accurate expression of the Federal antitrust laws or of congressional intent with regard to the application of such laws to resale price maintenance and other vertical restraints of trade. . . .*

Departments of Commerce, Justice, and State, the Judiciary and Related Appropriation Act, 1986, Pub. L. No. 99-180, 99 Stat. 1136, 1169-70 (1985).[12] Thus, Congress only two years ago *explicitly rejected* the very same restriction on applying the *per se* rule against vertical price fixing—that there must be an agreement to set prices at some level—created by the Fifth Circuit's decision in this case.

When confronted with a longstanding statutory construction that Congress has consistently refused to disturb, even when revisiting this specific area of the law, *Square D Co. v. Niagara Frontier Tariff Bureau, et al.*, 106 S. Ct. 1922, 1927-28 (1986), this Court has consistently and properly deferred to congressional intent, rather than itself engaging in the formulation of national economic policy. *See Arizona v. Maricopa County Medical Society*, 457

12. On December 9, 1985, the House of Representatives also passed a House Resolution, H.R. Res. 303, criticizing the Guidelines for "qualifying the accepted rule that vertical price fixing in any context is illegal *per se*." The House Judiciary Committee's Report accompanying H.R. Res. 303 disavows the Guidelines' view on vertical price fixing as an attempt to "dilute or trivialize the generality of the *per se* rule against price fixing, both horizontal and vertical." House Judiciary Committee's Report on Vertical Restraints Guidelines Resolution, H.R. Rep. No. 99-399, 99th Cong., 1st Sess. 6, *reprinted in* 49 Antitrust & Trade Regulation Report (BNA) 952, 956 (Nov. 28, 1985).

U.S. at 355, n.30 ("[Congress] can, of course, make *per se* rules inapplicable in some or all cases, and leave courts free to ramble through the wilds of economic theory in order to maintain a flexible approach", quoting *United States v. Topco Associates, Inc.*, 405 U.S. 596, 610, n.10 (1972)).

In *Square D* this Court was asked to overturn *Keogh v. Chicago & Northwestern R. Co.*, 260 U.S. 156 (1922), holding that Interstate Commerce Commission approval of tariff rates fixed in violation of the antitrust laws does not give rise to a private treble-damage action under Section 7 of the Sherman Act. Petitioners argued, among other things, that *Keogh's* ban on treble-damage actions was inconsistent with the policies underlying subsequent legislation affecting interstate carriers under the antitrust laws, although such legislation had not explicitly overruled *Keogh*.[13] The Court rejected that argument, stating that, even assuming *Keogh* was unwise as a matter of policy, it should not be abandoned without explicit legislative action by Congress. 106 S. Ct. at 1928. The Court reasoned that because Congress had addressed this area of the law in subsequent legislation and had left the *Keogh* rule undisturbed, it was inappropriate for the Court to take the initiative in effect what would amount to a statutory amendment:

> Particularly because the legislative history reveals clear congressional awareness of *Keogh* . . . the fact that Congress specifically addressed this area and left

13. Petitioners in *Square D* relied on the 1948 Reed-Bulwinkle Act, Pub. L. No. 80-662, 62 Stat. 472 (1948) (current version at 49 U.S.C. § 10706), and the Motor Carrier Act of 1980, Pub. L. No. 96-296, 94 Stat. 793, delineating an antitrust immunity for specific rate making activities.

> *Keogh* undisturbed lends powerful support to *Keogh's* continued viability.

Id.[14]

Id. See Jefferson County Pharmaceutical Ass'n v. Abbott Laboratories, 460 U.S. 150, 170 (1983) ("Although Congress is aware of these criticisms, the [Robinson-Patman] Act has remained in effect for almost half a century. And it certainly is 'not for [this Court] to indulge in the business of policy-making in the field of antitrust legislation' . . .", quoting *United States v. Cooper Corp.*, 312 U.S. 600, 606 (1941)).

This Court's refusal in *Square D* to overturn a long-standing statutory construction absent explicit congres-

14. Congress has amended the antitrust laws no less than a dozen times over the past decade without ever restricting of limiting the *per se* rule against vertical price fixing. *See*, Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801, discussed at pp. 4-7, *infra;* Hart-Scott-Rodino Antitrust Improvements Act of 1976, Pub. L. No. 94-435, 90 Stat. 1390; Federal Trade Commission Improvements Act of 1980, Pub. L. No. 96-252, 94 Stat. 374 (May 28, 1980); Soft Drink Interbrand Competition Act, Pub. L. No. 96-308, 94 Stat. 939 (July 9, 1980); Antitrust Procedural Improvements Act of 1980, Pub. L. No. 96-349, 94 Stat. 1154, 1980 U.S. Code Cong. & Admin. News 5144 (Sept. 12, 1980); Foreign Trade Antitrust Improvements Act of 1982, enacted as Title IV of the Export Trading Company Act of 1982, Pub. L. No. 97-290, 96 Stat. 1246 (Oct. 8, 1982); Damages Payable to Foreign States, Pub. L. No. 97-393, 96 Stat. 1964 (Dec. 29, 1982); Antitrust Procedures and Penalties Act of 1984 (Tunney Act), Pub. L. No. 93-528, 88 Stat. 1706; Shipping Act of 1984, Pub. L. No. 98-237, 98 Stat. 67 (Mar. 20, 1984) (amended title 46 of the United States Code to change terms of antitrust exemption for ocean shipping); National Cooperative Research Act of 1984, Pub. L. No. 98-462, 98 Stat. 1815 (Oct. 11, 1984); Local Government Antitrust Act of 1984, Pub. L. No. 98-544, 98 Stat. 2750 (Oct. 24, 1984); and Health Care Quality Improvement Act of 1986, enacted as Title IV of Pub. L. No. 99-660, 100 Stat. 3784 (Nov. 14, 1986) (creating antitrust damage exemption for medical peer review).

sional action is equally applicable to the case at bar. The Court's conclusion in *Square D* rests on the "strong presumption of continued validity that adheres in the judicial interpretation of a statute." 106 S. Ct. at 1930, n.34, citing *NLRB v. Longshoremen*, 105 S. Ct. 3045, 3058 (1985) ("[W]e should follow the normal presumption of *stare decisis* in cases of statutory interpretation"); *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 736 (1977) ("[W]e must bear in mind that considerations of *stare decisis* weigh heavily in the area of statutory construction, where Congress is free to change this Court's interpretation of its legislation").[15] This presumption of *stare decisis* is further strengthened where, as in the present case, Congress has addressed the area of law at issue without changing the precedent established by the Court:

> We are especially reluctant to reject this presumption in an area that has seen careful, intense, and sustained congressional attention. If there is to be an overruling of the *Keogh* rule, it must come from Congress, rather than from this Court.

106 S. Ct. at 1931.

Congress has consistently and vigorously supported continued application of a broad *per se* rule against vercal price fixing. As indicated above, Congress has amend-

15. The Court in *Square D* aptly quoted Justice Brandeis, the author of the opinion in *Keogh*, commenting later upon the presumption of continuity in statutory interpretation:

> *Stare decisis* is usually the wise policy because in most matters, it is more important that the applicable rule of law be settled than that it be settled right. . . . This is commonly true, even where the error is a matter of serious concern, provided correction can be had by legislation.

106 S. Ct. at 1931; quoting Burnet v. Coronado Oil & Gas Co., 285 U.S. 393, 406 (1932) (Brandeis, J., dissenting).

ed the antitrust laws no less than twelve times during the last decade without qualifying the *per se* rule one iota. Congress has also recently stated in no uncertain terms its rejection of any requirement to fix prices "at some level" for application of the *per se* rule against vertical price fixing. Departments of Commerce, Justice and State, the Judiciary and Related Agencies Appropriation Act, 1986, *supra*.[16]

The Court should follow its own precedents and require that any effort to restrict application of the *per se* rule to vertical price fixing under the Sherman Act be addressed to Congress rather than to this Court.

V. Conclusion.

It has been said that "Realities must dominate the judgment. . . . The Anti-Trust Act aims at substance." *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. at 47, quoting *Appalachian Coals, Inc. v. United States*, 288 U.S. 344, 360, 377 (1933) (Hughes, C.J.). The reality here is that BEC was terminated by an agreement between Sharp and Hartwell for the purpose of eliminating price competition. The Fifth Circuit ignored the obvious anticompetitive purpose of this agreement and

16. For the past several years, Congress has even gone so far as to prohibit the Department of Justice from using appropriated funds for "any activity to alter the *per se* prohibition on resale price maintenance", including appearances in court. Section 605 of the Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriation Act, 1987, enacted into law as part of the Continuing Appropriations, 1987, Pub. L. No. 99-591, ____ Stat.____. Notably excepted from this prohibition, however, is the Justice Department's activity before Congress, reflecting Congress's view that it is the proper forum in which to address any changes in this area of the law and not the courts.

created, against all precedent and common sense, a requirement that the *per se* rule will not apply unless Sharp and Hartwell also agreed to set prices "at some level". This requirement has been rejected by the decisions of this Court and by Congress. It is furthermore a nonsensical requirement because it assumes that without such an agreement the surviving distributor remains theoretically "free" to discount if he pleases, ignoring the fact that such a distributor will ordinarily use that freedom to raise his prices or his profit margins, which is precisely what occurred in the present case.

This Court once stated that it did not

> propose to construe the Sherman Act to prohibit conspiracies to fix prices at which competitors may sell, but to allow conspiracies or combinations to put competitors out of business entirely.

United States v. General Motors Corp., 384 U.S. at 148. The Court should follow its precedents and reverse the Fifth Circuit's decision below.

Respectfully submitted,

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No. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR RESPONDENT SHARP ELECTRONICS CORPORATION

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QUESTION PRESENTED

Should an alleged agreement between a supplier and a full service dealer to terminate a free riding discounter—which agreement does not restrict the pricing freedom of any dealer—be deemed a form of price fixing unlawful *per se* under the Sherman Act?

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No. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR RESPONDENT SHARP ELECTRONICS CORPORATION

COUNTERSTATEMENT OF THE CASE

Introduction

While the narrow issue in this case is the proper definition of vertical price fixing under section 1 of the Sherman Act, 15 U.S.C. § 1, this case also raises issues of immense practical importance in the marketplace. The Court's decision will determine whether a supplier is able to protect its distribution system from "free riders" who reap the benefits of the efforts, but assume none of the costs, of full service dealers who provide the advertising, promotional, educational and point-of-sale services needed to benefit the consumer and stimulate sales of the supplier's product.

In 1973, Sharp Electronics Corporation ("Sharp"),[1] a supplier of business equipment, terminated Business Electronics Corporation ("BEC") as a Sharp dealer in Houston. The termination came about because BEC was a free rider: it had no salespeople,

1. Pursuant to Rule 28.1 of the Supreme Court Rules, Sharp Electronics Corporation represents that its parent corporation is Sharp Corporation and that it has no subsidiaries or affiliates.

did no advertising, and engaged in no promotional or educational services to stimulate sales. Gilbert Hartwell, Sharp's other Houston dealer, did all of these things, but once Hartwell developed a customer, BEC would take the sale by using its lower costs to offer that customer a price no full service dealer like Hartwell could afford to meet. Hartwell eventually gave Sharp an ultimatum that unless BEC was terminated, Hartwell would resign as a Sharp dealer. It was only then that Sharp terminated BEC's dealership.

BEC maintains that Hartwell's ultimatum and Sharp's acquiescence in it were motivated by concerns over the low prices BEC's free riding enabled it to charge, and that its termination therefore constituted a *per se* illegal vertical price fixing agreement. BEC makes this claim even though it does not deny that it was free riding, and even though it did not allege that there was any agreement between Sharp and Hartwell as to the prices Hartwell would charge if BEC were terminated.

The United States Court of Appeals for the Fifth Circuit concluded that a supplier is entitled to protect its distribution system, and that terminating a free rider at the request of a competing dealer is not *per se* illegal, so long as there is no agreement between the supplier and the remaining dealer as to the prices the latter will charge after the termination. Pet. App. at 13a-14a.[2] It is this determination that BEC challenges.

The Parties And The Market

Respondent Sharp is the supplier of a wide variety of Sharp brand consumer and business products, including electronic calculators. Sharp distributes these products throughout the United States. Tr. 1324-25.[3]

In 1968, Kelton Ehrensberger became the sole authorized dealer for Sharp electronic calculators in the Houston, Texas

2. "Pet. App." refers to the Petition for Writ of Certiorari which contains the majority and concurring opinions of the court of appeals. These opinions are also reported in *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 780 F.2d 1212 (5th Cir. 1986), *cert. granted*, 107 S. Ct. 3182 (1987).

3. "Tr." refers to the trial transcript.

area. Tr. 58; 68-69. Ehrensberger subsequently incorporated BEC and continued the dealership under that name. Tr. 58-59.

When Ehrensberger became a Sharp dealer, electronic calculators were new in the market and were not the compact, familiar and inexpensive items they are today. Rather, these calculators were large, complicated products that were designed for use by commercial enterprises, and that sold at retail for up to $1,000 per unit. Tr. 59-61; 153; 342-43; 1106-07. Initially, electronic calculators competed with large, electro-mechanical calculating machines manufactured by established companies such as Monroe, Canon, Victor and Freiden. Tr. 356; 358-59.

Because electronic calculators were expensive, complex and unfamiliar, stimulating buyer interest required extensive promotional and educational efforts by both the supplier and the dealer. This was necessary, first, to convince the customer to buy an electronic calculator rather than the more familiar mechanical kind and, second, to enable the customer who decided to purchase an electronic calculator to determine which model would suit his particular needs. Typically, a dealer would have to make four or five sales calls on a single customer before that customer could be persuaded to place an order. Tr. 113-14; 343-48; 1429-32.

BEC did not emphasize the kind of pre-sale educational and promotional services that Sharp desired and that were necessary to stimulate consumer interest and effect sales. Instead, BEC's marketing strategy was to concentrate on discount prices. Tr. 72-73; 124-28. The net result of this strategy was that, by 1972, even though there was no other authorized Sharp dealer in the Houston area, BEC was falling woefully short of the quota assigned by Sharp, *see* Defendant's Trial Exhibit ("Def. Ex.") No. 26 (introduced and admitted at Tr. 700), and Sharp decided to terminate BEC's dealership.[4] Tr. 827-30; Tr. 700.

4. BEC contends it was the fact that it priced below Sharp's suggested list, not its poor performance, that led Sharp to this decision, and that the jury agreed with BEC's contention. Brief of Petitioner Business Electronics Corporation ("BEC Br.") at 3, 7, 11, 31. However, BEC ignores the fact that the district court erroneously excluded on hearsay grounds contemporaneous business records showing Sharp's pre-existing policy to terminate *all* dealers whose

(footnote continued on following page)

Having reached this decision, Sharp began negotiations with Gilbert Hartwell of Hartwell's Office World to see if he would become the Sharp electronic calculator dealer in Houston. Tr. 321-22. Hartwell accepted with the understanding that BEC was to be terminated, and that Hartwell would have the exclusive Sharp dealership in the Houston area. Tr. 322-24.

Sharp did not terminate BEC, however, because a new Sharp management team assumed responsibility for the distribution of electronic calculators and wanted time to study the market before finally deciding on Sharp's distribution system in Houston. Tr. 1307-08; *see also* Tr. 830-33. As a result, from 1972 on, Hartwell and BEC both functioned as Sharp electronic calculator dealers in the Houston area.

This was not satisfactory from Hartwell's standpoint. From the inception, he complained repeatedly to Sharp that he had been promised an exclusive dealership and that Sharp's refusal to terminate BEC constituted a breach of that promise. Tr. 272-73; 323. But notwithstanding its earlier assurances, Sharp refused to terminate BEC. Tr. 269.

BEC's retention might have been a bitter pill for Hartwell, but the Hartwell appointment yielded an unexpected dividend for BEC. BEC quickly discovered that it could profitably dispense with its own sales force and free ride on Hartwell's sales efforts. *See, e.g.*, Tr. 283-84; 346-48.

(footnote continued from previous page)
performance against quota was as poor as BEC's. Pet. App. at 15a-18a. These documents were so clear in their import, even the district court observed that if they were admitted:

> [T]hat's going to knock the plaintiff out of the suit. He couldn't win.
>
> . . . .
>
> I haven't seen anything in this case that's so damaging to the plaintiff as all these papers saying fire anybody — that's what they say — fire anybody who [does not] meet that standard.

Tr. 811; *accord, e.g.*, Tr. 798.

The court of appeals ruled that these documents must be admitted at a new trial. Pet. App. 15a-18a. BEC's assertions, then, as to what the jury found regarding Sharp's motivation in terminating BEC must be read in light of the fact that the jury was deprived of evidence crucial to Sharp's defense.

BEC was able to free ride because Hartwell ran a full service dealer operation. Hartwell advertised the Sharp product extensively and had a trained sales staff that would spend time with prospective customers discussing their needs, explaining the merits of the new electronic calculator, demonstrating different models of calculators and performing the other expensive pre-sale promotions and services necessary to generate interest in electronic calculators in general and in the Sharp model in particular. Tr. 343-44; 1031; 1102-03.

Before Hartwell became a dealer, BEC had to perform these services itself and bear the attendant costs if it was to make any sales. Tr. 112-114. Once Hartwell assumed this burden, however, BEC dispensed with its entire sales force, stopped advertising, and let Hartwell's salespeople educate prospective customers at Hartwell's expense. When a customer was convinced that he should purchase an electronic calculator and knew what model would fit his needs, BEC would procure the sale by a flier offering that very customer a price so low that Hartwell, a full service dealer with expenses for advertising and salespeople salaries, could not possibly meet it. Tr. 110; 279-80; 283-84; 343-44; 346-48.

Recognizing that he was subsidizing BEC's sales and in effect competing against himself, Hartwell complained bitterly to Sharp. Tr. 279-80. Hartwell stated that he did not care what BEC charged to customers BEC developed on its own, but Hartwell did not want to see customers that he had discovered and educated snatched away because BEC, with no sales staff and service costs, could offer a much lower price:

> Q. So, when you talked yesterday about your unhappiness about Mr. Ehrensberger's discounting or price cutting what was it exactly that you were upset about, was it the fact that he was selling calculators at below list price?
>
> A. No.
>
> Q. What was it?
>
> A. It was the fact we were working the deal, doing all the work and we weren't getting any of the profit. We

were going off—Mr.Ehrensberger's flier just cut your legs out from under you. We did all the legwork, all the selling and one little piece of flier came in and they are ready to buy the same product from him.

Q. Did you care what price Mr. Ehrensberger offered to customers that he developed?

A. I could care less.

Tr. 347-48; *accord, e.g.*, Tr. 284.

Sharp responded to Hartwell's complaints by saying that it believed there was simply nothing it could do to restrict BEC's ability to sell as it wanted, at whatever price it wanted. In fact, Hartwell complained that all he ever heard from Sharp was "the same broken record, that a manufacturer could not tell a dealer what to sell his product for[.] [N]o matter who I talked to . . . . I heard that over and over." Tr. 366; *accord, e.g.*, Tr. 351-53; 363-65; 366-67; 867-68; 918-22.

Therefore, in June 1973 Hartwell presented an ultimatum: if Sharp wanted to retain Hartwell as a dealer, it would have to be on the exclusive basis originally promised—within 30 days Sharp would have to terminate BEC or Hartwell. Tr. 367-72; 420; 441; *see also* Tr. 290.

From an objective business standpoint, this was not a difficult decision. Prior to 1972, when BEC serviced the Houston market alone, its performance was so dismal as to warrant termination under Sharp's pre-existing standards. Tr. 827-30; Def. Ex. No. 26 (introduced and admitted at Tr. 700); Tr. 199-200; *see also* Tr. 768; 773-74; 840-41; Def. Ex. No. 6 (introduced and admitted at Tr. 839-40). Even when Hartwell and BEC both functioned as dealers and BEC was able to free ride, Hartwell's performance had generally been superior. Tr. 844-45; Def. Ex. No. 108 (introduced and admitted at Tr. 843-44).

Most importantly, Hartwell had a professional sales staff to provide necessary services to potential customers. BEC no longer had any sales force, and without the ability to free ride upon a full service dealer like Hartwell, BEC would have no capacity whatsoever to service the territory. In view of the fact that Hartwell had a great deal more potential for future growth,

Sharp chose to retain Hartwell and terminated BEC's dealership. Tr. 371-74; 774-75; 842-45; 867; 1309. BEC then commenced suit.

Proceedings In The District Court

BEC acknowledged at trial that its *sole* claim was that it had been terminated pursuant to a vertical price fixing agreement between Sharp and Hartwell. Tr. 668-70. However, BEC did not maintain that either before or after its termination Sharp and Hartwell actually fixed prices. In other words, BEC did not contend that Sharp told Hartwell what prices to charge, nor did it contend that Hartwell ceded to Sharp any part of his discretion to price as he chose. Rather, BEC maintained that so long as Sharp terminated BEC because of its discounting, this was vertical price fixing and *per se* illegal:

> Mr. McGowan [counsel for BEC]: We do not—plaintiff; in this type of case, a vertical price fixing case, does not have to prove an agreement between Sharp and somebody else to fix retail prices to agree on specific prices. What we have to prove, your Honor, is there was an agreement to terminate the dealer because it was discounting. . . .
>
> . . . .
>
> . . . That's our theory, your Honor, that he was terminated at the request of Mr. Hartwell because he was discounting. Hartwell didn't like his price cutting, so he went to Sharp and asked he been *[sic]* terminated, Sharp agreed to, he was terminated.
>
> The Court: Is that the only theory you want me to present to the jury?
>
> Mr. McGowan: That's our theory, your Honor.

Tr. 668-69.

BEC's invention of a theory of vertical price fixing that did not require any proof of an agreement on price was a creature of necessity. The uncontroverted evidence at trial showed there was no agreement on prices or price levels. Tr. 327; 371-73; *reprinted*

in J.A. 8-11; *see also* J.A. 12-13.[5] Hartwell testified that both before and after the termination he understood that he could sell at whatever prices he wanted, Tr. 332, he sold at whatever prices he wanted, Tr. 333, and he regularly sold at prices well below those recommended by Sharp. In Hartwell's words, he discounted on the sales of Sharp calculators virtually every day with no interference by Sharp, and after the BEC termination, the retail prices for Sharp calculators actually decreased. Tr. 294; 327; 342-43; 893-94; *see also* Tr. 1027-28; 1105.

The record also shows that interbrand competition in the relevant market was, and remains, fierce. During the time period here involved, some 100 competing brands of calculators were being sold, and there was never any suggestion at trial that Sharp had a significant share of any interbrand product market. Tr. 931.[6] Moreover, during the ten year period prior to the trial, not only did Hartwell's prices decrease, but the average retail price of calculators also decreased substantially. Tr. 893-94; 931; 1024; 1027-28.[6]

The District Court's Instructions To The Jury

Since BEC charged Sharp with terminating BEC's dealership pursuant to a price fixing agreement, Sharp requested the district court to instruct the jury that to find a violation of section 1 of the Sherman Act, it would first have to find that Sharp and Hartwell had some agreement as to the prices or price levels Hartwell

5. "J.A." refers to the Joint Appendix.

6. BEC complains throughout its brief that Hartwell's gross profit margin increased after BEC's termination and that this is somehow evidence of *per se* illegal conduct. BEC Br. at 5 & n.3, 19, 43. But gross profit margin as defined in this case is simply the difference between the dealer's cost of purchase from the supplier and its sales price to the consumer. Tr. 381; BEC Br. at 5. It says nothing about the price paid by the consumer and, moreover, with respect to a full service dealer like Hartwell, who incurs substantial service and promotional expenses, it says nothing about the profits actually realized by the dealer.

If anything, the fact that Hartwell's gross profit margin increased after BEC's termination is perfectly illustrative of the proper operation of the marketplace. Uninhibited by free riding, a full service dealer is able to invest in more and better consumer services and recoup that investment through the necessary price adjustments to the consumer. *See infra* pp. 28-33.

would charge after the BEC termination. *See* J.A. 7 (Defendant's Requested Jury Instruction No. 23).

The district court refused to give this instruction, and over Sharp's objection, Tr. 1594-95; 1598-99, instructed the jury that:

> The Sherman Act is violated when a seller enters into an agreement or understanding with one of its dealers to terminate another dealer because of the other dealer's price cutting.

J.A. 18.

The district court also submitted a special interrogatory to the jury:

> Question Number 1 asks you whether you find by a preponderance of the evidence that there was an agreement or understanding between Sharp and Hartwell to terminate Business Electronics as a Sharp dealer because of Business Electronics' price cutting.

J.A. 16.

Sharp objected to this instruction because it did not require any finding of price fixing as a predicate for liability.[7] The jury answered "yes" to Question Number 1 and returned a verdict in favor of BEC in the amount of $600,000. Tr. 1614.

7. Amicus Curiae National Mass Retailing Institute ("NMRI") argues that this instruction substantially complied with Sharp's own Requested Jury Instruction No. 24. Brief Amicus Curiae of National Mass Retailing Institute in Support of Petitioner ("NMRI Br.") at 20-23. NMRI's argument ignores what the record makes obvious – that Sharp's Requested Jury Instruction No. 24 was intended to be given in tandem with its Requested Jury Instruction No. 23, which, as shown above, required that there be an agreement to fix or maintain resale prices at a certain level. Sharp made it clear that the two instructions were intended to be read together when it objected to the district court's proposal to charge the jury in accordance with BEC's theory. Tr. 1597-98. The best evidence of Sharp's intention in this regard is the fact that BEC, which was present at the trial, has itself not seen fit to raise this specious argument before either the court of appeals or this Court.

The Court Of Appeals Opinion

The court of appeals reversed. Pet. App. at 18a-19a. Relying on *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984), it concluded that BEC's theory of *per se* illegality would proscribe conduct of the kind permitted—indeed encouraged—by the antitrust laws:

> [T]he manufacturer which desires to terminate a price cutter because of its free riding will be deterred from this legitimate action because it is indistinguishable, except perhaps to a mind reader, from what [BEC maintains the law] prohibits, i.e., termination of a price cutter because of its price cutting.

Pet. App. at 12a.

Accordingly, the court of appeals held that the jury should have been required to find that BEC was terminated pursuant to a price maintenance agreement between Sharp and Hartwell before it was permitted to find a *per se* violation of section 1 of the Sherman Act. Pet. App. at 12a. The court did *not*, as BEC now claims, BEC Br. at 8-9, require an *express* finding that prices be fixed at a defined level. Rather, it held that no price fixing agreement could be said to exist unless the dealer ceded to the supplier its right to price at whatever level it chose in the exercise of its own independent business judgment:

> [I]n order for a manufacturer's termination of a distributor to be illegal *per se*, it must be pursuant to a price maintenance agreement with another distributor. That distributor must expressly or impliedly agree to set its prices at some level, though not a specific one. The distributor cannot retain complete freedom to set whatever price it chooses.

Pet. App. at 13a-14a. Because the jury instructions failed to reflect this standard, the court of appeals held them critically

defective, thus requiring reversal of the judgment.[8] Pet. App. at 13a-14a.

However, the court of appeals also found that even though Hartwell testified that he always priced at whatever level he wanted, the jury could infer that his pricing policies were in fact undertaken pursuant to a *per se* illegal resale price fixing agreement with Sharp, based on the fact that Hartwell frequently priced in conformity with Sharp's suggested list. Pet. App. at 15a. For this reason, the court remanded for a new trial under proper jury instructions. Pet. App. at 18a-19a.

Judge Jones concurred, but she stated that this case perfectly illustrates why all vertical restraints, including vertical price restraints, should be tested under the rule of reason. She therefore urged this Court to overturn the rule of *per se* illegality for vertical price restraints. Pet. App. at 19a, 23a.

INTRODUCTION AND SUMMARY OF ARGUMENT

BEC's argument in this Court is devoted largely to the proposition that price fixing is evil and that vertical price fixing agreements should therefore remain *per se* illegal. The primary issue in this case, however, is *not* whether vertical price fixing violates the antitrust laws, but whether a specific kind of agreement—a supplier's agreement to terminate a discounting dealer—constitutes vertical price fixing. BEC begs this question because the court of appeals' determination that such an agreement is not, of itself, *per se* illegal is demonstrably correct.

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8. As noted above, *supra* note 4, the court of appeals also ruled that the district court improperly excluded evidence crucial to Sharp's defense. Pet. App. at 15a-18a. For this reason, BEC is wrong when it states that the district court's judgment should be reinstated. BEC Br. at 11. Even if BEC's jury instructions had not been critically defective, a new trial would have been required because of this improper exclusion of evidence.

I.

This Court consistently has held that the *per se* rule is reserved for a narrow category of practices that always or nearly always have a "pernicious effect on competition and lack of any redeeming virtue." *Northern Pacific Railway* v. *United States*, 356 U.S. 1, 5 (1958). BEC attempts to invoke the *per se* rule simply by labeling Sharp's conduct as pernicious, without engaging in any meaningful effort to analyze its effects on competition. However, *Continental T.V., Inc.* v. *GTE Sylvania Inc.*, 433 U.S. 36 (1977), establishes that most supplier-dealer agreements—even those that increase resale prices—are pro-competitive in nature. They can be used to encourage dealers to make an investment in the supplier's product and provide expensive promotion, education and other customer services that benefit the consumer and stimulate sales of the supplier's product. Thus, they should not be summarily condemned.

Economic analysis confirms that the specific conduct at issue here—the termination of a discounting dealer who undermines a supplier's product distribution system by engaging in free riding—serves to enhance efficiency and to stimulate interbrand competition. Efficient and pro-competitive product distribution depends on efforts by dealers to provide a variety of services, such as consumer education and product demonstration. Too frequently, discounting dealers do not provide these services, even when they are required for an effective distribution system. Instead, as the evidence in this case illustrates, these dealers will "free ride" on the efforts of responsible dealers who do provide these services; that is, they will wait until another dealer, at his own expense, stimulates consumer demand and then use their lower sales costs to undercut the full service dealer's prices and steal the sale.

This Court reaffirmed in *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984), that a vertical price fixing agreement does not exist simply because a particular practice may affect resale prices. Rather, *Monsanto* holds that such an agreement exists only where a dealer cedes its right to price in accordance with its independent business judgment and agrees to charge a price dictated by the supplier. A supplier's agreement to terminate a free riding dealer says nothing about what prices the remaining dealer will charge. Thus, the court below properly concluded that the jury was erroneously instructed on the elements of a *per se* violation of section 1 of the Sherman Act when the district court charged that an agreement to terminate a discounting dealer, standing alone, violates section 1.

II.

BEC proposes that the law be changed, and that all agreements to terminate discounters, even absent any agreement on prices between the supplier and the remaining dealer, be deemed *per se* illegal. Since free riders are, by definition, discounters, BEC's rule would make it a virtual certainty that a jury verdict in favor of the terminated dealer must be returned, even where, as in this case, the supplier has done nothing more than or different from that which is permitted by *Sylvania*.

Sylvania recognizes that a system of pro-competitive vertical restraints cannot be achieved unless the supplier is free to limit its distribution system by, for example, providing one dealer with an exclusive territory. BEC offers no rationale for making a supplier's decision to terminate a free riding dealer *per se* illegal even though a decision to grant an exclusive dealership—which would accomplish the same economic purpose and effect—is not.

The reason that BEC makes no attempt to examine the economic purpose or effect of agreements such as the one at issue is because this examination would show that agreements to terminate a discounter are not inherently anticompetitive. To the

contrary, they are generally valuable competitive tools, particularly where a supplier's efficient distribution system is threatened by a free rider. Such agreements should not be deemed illegal *per se* without any consideration of their beneficial effects on interbrand competition in the marketplace.

III.

Finally, the judgment below may also be affirmed on the ground that vertical price restraints, like all other vertical restraints, should be subject to the rule of reason. Vertical price restraints have precisely the same pro-competitive features as non-price vertical restraints. They can be used to promote dealer services by ensuring that the dealer will be able to charge a price high enough to recoup his investment in those services. At the same time, built-in marketplace checks—most importantly, the presence of interbrand competition—minimize any risk that such restraints will have an adverse effect on competition. Moreover, in many circumstances, non-price vertical restraints will not be an effective means of dealing with a free rider problem; only a resale price maintenance agreement will work.

In order to ensure a rational body of antitrust law and curtail the ever-swelling flow of dealer termination cases, vertical price restraints should be reviewed under the same standard as vertical non-price restraints, that is, they should be subject to the rule of reason.

ARGUMENT

POINT I

AN AGREEMENT BETWEEN A SUPPLIER AND A DEALER TO TERMINATE A COMPETING DEALER BECAUSE OF ITS DISCOUNTING IS NOT *PER SE* ILLEGAL ABSENT AN AGREEMENT ON PRICE

A. A *Per Se* Illegal Vertical Price Fixing Agreement Exists Only If There Is A Supplier-Dealer Agreement on Price

Under *Continental T.V., Inc.* v. *GTE Sylvania Inc.*, 433 U.S. 36 (1977), only vertical price fixing agreements are *per se* illegal. All other vertical restraints are tested by the rule of reason, which measures the actual market impact of an alleged restraint in the individual circumstances of the case.

At trial, BEC did not try to prove a rule of reason case. BEC could not do so because the factual record in this case shows that all the benefits of healthy competition—more competing brands, better product mix, lower prices—have been fully realized in the electronic calculator market that Sharp served. *See* Pet. App. at 19a-23a.

Recognizing that it can prevail only if it established a *per se* claim, BEC maintains that the court of appeals radically re-wrote the antitrust laws in holding that an agreement between a supplier and one of its dealers to terminate a discounting dealer is not, of itself, a price fixing agreement. According to BEC, it was a "novel departure from the standard of *per se* illegality" for the court below to hold that proof of a supplier-dealer agreement to set resale prices was an integral element of a *per se* illegal vertical price fixing agreement. BEC Br. at 11. BEC contends that this Court's decisions establish that *any* agreement intended to reduce or eliminate price competition constitutes price fixing, even if no agreement on prices exists. BEC Br. at 9-11, 12, 15-19, 21.

BEC is incorrect. This Court has recognized that supplier-dealer agreements frequently stimulate interbrand competition

and that a vague or overbroad definition of vertical price fixing—of the type proposed by BEC—is likely to deter pro-competitive conduct. *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752, 762-64 (1984).[9] Accordingly, this Court has always employed the careful, focused definition of price fixing followed by the court below. It has applied the *per se* rule only when the evidence showed that a dealer had ceded his right to price independently:

> This Court has applied the *per se* rule against resale price maintenance only to situations in which the evidence showed that the manufacturer or wholesaler "dictat[ed] the prices charged by" a wholesaler or retailer. *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc.*, 445 U.S. [97,] 103 [(1980)]. . . .

Brief for the United States as Amicus Curiae on BEC's Petition and Sharp's Cross-Petition for Writ of Certiorari (hereinafter cited as "U.S. Br.") at 8 (approving the analysis of the court of appeals) (additional citations omitted). *Accord United States* v. *A. Schrader's Son, Inc.*, 252 U.S. 85, 99 (1920) (recognizing the "obvious difference between the situation presented when a manufacturer merely indicates his wishes concerning prices . . . and one where he enters into agreements which undertake to bind [dealers] to observe fixed resale prices").[10]

9. Even in the horizontal context, this Court has counseled against application of the *per se* rule based upon an overbroad definition of price fixing, stating that much conduct that could fall within a literal and overly simplistic definition of the term is conduct that should not be summarily condemned under section 1 of the Sherman Act. *Broadcast Music, Inc.* v. *CBS*, 441 U.S. 1, 8-10 (1979).

10. This standard has been applied by numerous lower courts as well. *See, e.g., AAA Liquors, Inc.* v. *Joseph E. Seagram & Sons, Inc.*, 705 F.2d 1203, 1205-06 (10th Cir. 1982), *cert. denied*, 461 U.S. 919 (1983); *Muenster Butane, Inc.* v. *Stewart Co.*, 651 F.2d 292, 295-96 (5th Cir. 1981); *Borger* v. *Yamaha Int'l Corp.*, 625 F.2d 390, 397 (2d Cir. 1980) (reversing jury verdict of *per se* liability based on jury instruction substantially identical to BEC's); *Chisholm Bros. Farm Equip. Co.* v. *International Harvester Co.*, 498 F.2d 1137, 1142 (9th Cir.) ("The crux of any price-fixing agreement is the relinquishment by a trader . . . of the freedom to set prices in accordance with his own judgment."), *cert. denied*, 419 U.S. 1023 (1974).

BEC attempts to harmonize its argument with this established precedent by asserting that the only purpose and effect of a supplier's agreement to terminate a discounter is to permit the remaining dealer to raise its prices. Indeed, BEC goes so far as to argue that termination in these circumstances necessarily implies that the remaining dealer has agreed to charge a price higher than that of the terminated dealer, and that it is illogical to believe that the dealer whose complaints led to the termination of a discounting competitor will then start to discount himself. BEC Br. at 9-10; 19-21; 43.

These arguments are facile, but they do not withstand scrutiny. A supplier's termination of a discounting dealer may be done for a variety of reasons wholly unrelated to control of the remaining dealer's prices. For example, it may be done to provide the remaining dealer with an exclusive territory or to avoid a free riding problem—reasons that are perfectly lawful and economically beneficial and that, absent an actual agreement on prices, should not be interdicted by section 1 of the Sherman Act. *Monsanto*, 465 U.S. at 762-64; *Sylvania*, 433 U.S. at 54-57; *Valley Liquors, Inc.* v. *Renfield Importers, Ltd.*, 822 F.2d 656, 663-64 (7th Cir. 1987). Thus, contrary to BEC's principal submission, the circumstance of termination of a discounter standing alone cannot be equated with an effort on the supplier's part to control its dealer's prices.

Moreover, contrary to BEC's secondary argument, it is perfectly normal for a dealer who complains about another dealer's discounting to continue discounting after the latter's termination. In fact, that is precisely what Hartwell did here. Tr. 294; 327; 332; 333; 342-43; 893-94; 1027-28; 1105. *See also Valley Liquors*, 822 F.2d at 662. This is simply because an agreement to terminate a discounter says nothing about any price agreement between the supplier and the remaining dealer.

Accordingly, to infer an agreement to fix prices from the mere circumstance of an agreement to terminate a discounter, with no evidence that anyone ever charged a price dictated by the supplier, would be to find price fixing by speculation. This would

constitute a perversion, rather than a proper application, of section 1. *Monsanto*, 465 U.S. at 763-64; *Matsushita Electric Industrial Co.* v. *Zenith Radio Corp.*, 475 U.S. 574, 106 S. Ct. 1348, 1361-62 (1986).

This point is also confirmed by the very decisions upon which BEC purports to rely. For example, in *United States* v. *Parke, Davis & Co.*, 362 U.S. 29, 43 (1960), *cited in* BEC Br. at 9, 13 n.6, 16-18, 22, this Court held that absent direct evidence of an agreement on prices, plaintiff must be able to show, at a minimum, that remaining dealers charged a price directed by the supplier, or no vertical price fixing agreement can be inferred. As the court in *Yentsch* v. *Texaco, Inc.*, 630 F.2d 46 (2d Cir. 1980), summarized the rule flowing from *Parke, Davis* and *Albrecht* v. *Herald Co.*, 390 U.S. 145 (1968):

> The required combination must be demonstrated, then, by proof of (1) an express or implied agreement, or (2) the securing of actual adherence to prices by means beyond mere refusal to deal. . . .Thus, [plaintiff] might satisfy the [test] by proving either that *he* complied with [defendant's] price policy, or that the price policy (1) was firmly enforced, (2) applied to all service station dealers, and (3) was acquiesced in by most of them. Taken together, then, *Parke, Davis* and *Albrecht* stand for the basic proposition that use of coercion that achieves actual price-fixing is illegal.

Yentsch, 630 F.2d at 52.[11]

These critical elements of a vertical price fixing agreement—the requirement that the dealer cede his independence and enter into an actual agreement on prices with the supplier, as well as the requirement that remaining dealers adhere to the supplier's price demands—were synthesized by this Court in *Monsanto*.

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11. BEC similarly distorts the holding of *United States* v. *Bausch & Lomb Optical Co.*, 321 U.S. 707, 721 (1944). *See* BEC Br. at 17. In *Bausch & Lomb*, this Court stated that a distributor of a trade-marked article may not lawfully limit the price at which its purchaser may resell by an agreement between the seller and purchaser to maintain resale prices. 321 U.S. at 721. The Court did *not*, as BEC suggests, hold that *per se* liability may be imposed absent a price fixing agreement.

Monsanto, like this case, involved a claim of price fixing predicated upon the fact that complaints from other dealers about plaintiff's discounting resulted in the supplier's termination of plaintiff. Remarkably, BEC asserts that *Monsanto* concerned only the question of what proof was required to establish concerted action sufficient under *United States* v. *Colgate & Co.*, 250 U.S 300 (1919), and not the distinction between *per se* illegal agreements on price and other types of concerted activity. BEC Br. at 23. BEC is wrong.

In *Monsanto*, this Court emphasized that a crucial distinction to be drawn "in distributor-termination cases is that between concerted action to set prices and concerted action on non-price restrictions." *Monsanto*, 465 U.S. at 761. The Court stated that vertical price fixing exists only if the evidence shows that the supplier "and some of its distributors were parties to an 'agreement' or 'conspiracy' to maintain resale prices and terminate price cutters." *Id.* at 765. The Court continued that if "there was evidence of an agreement with one or more distributors to maintain prices, the remaining question is whether the termination of [the price cutting distributor] was part of or pursuant to that agreement." *Id.* at 767. Finally, the Court stated that for plaintiff to prove the requisite agreement, it must demonstrate that "distributors are not making independent pricing decisions," *id.* at 762, and must show not only that the distributor conformed to the suggested price, but "that the distributor communicated its acquiescence or agreement [to the suggested price], and that this was sought by the manufacturer." *Id.* at 764 n.9.

The court of appeals correctly applied these principles in the instant case. The simple truth is that BEC did not present any evidence at trial with respect to the essential elements of a vertical price fixing agreement. BEC made no attempt to show that Hartwell ceded any of his ability to price independently. In fact, BEC expressly eschewed at trial any claim that Sharp and Hartwell entered into any agreement, direct or indirect, as to the prices Hartwell would charge after the BEC termination. Tr. 668-70.

In short, BEC failed to establish any of the elements that Monsanto requires for there to be a per se illegal price fixing agreement. Accordingly, the court of appeals' determination that no vertical price fixing agreement existed in this case was unquestionably correct. *See generally* U.S. Br. at 10-12 (agreeing with the court of appeals' analysis).

B. An Agreement Between A Single Supplier And A Single Dealer To Terminate A Competing Dealer Because Of Its Discounting Is Not A Horizontal Group Boycott

Having failed to show that a supplier's agreement to terminate a discounting dealer constitutes vertical price fixing, BEC attempts to avoid *Monsanto* by asserting that such an agreement can be viewed as a horizontal group boycott, *per se* illegal even absent evidence of price fixing. BEC Br. at 24-35.

BEC has come to its boycott theory late in the day. At trial, BEC explicitly stated that it was proceeding only on a vertical price fixing theory. Tr. at 668-70. BEC never sought an instruction to the jury based upon a horizontal group boycott theory, nor did it assert in the court of appeals that such a theory of liability constituted an alternative basis for affirming the district court judgment. Moreover, BEC did not raise this issue when it petitioned for certiorari. Accordingly, this segment of BEC's brief is not properly before the Court and should be disregarded. *See National Licorice Co.* v. *NLRB*, 309 U.S. 350, 357 n.2 (1940); Sup. Ct. R. 21.1(a); R. STERN, E. GRESSMAN & S. SHAPIRO, SUPREME COURT PRACTICE § 6.26, at 363-64 (6th ed. 1986).

In any event, BEC's horizontal group boycott argument is plainly wrong.

The instant case involves no horizontal element, only a single supplier-dealer agreement. A horizontal group boycott requires collaborative activity between two or more entities at the same level of competition. *Lomar Wholesale Grocery* v. *Dieter's Gourmet Foods*, 824 F.2d 582, 590 (8th Cir. 1987); *Westman Commission Co.* v. *Hobart International, Inc.*, 796 F.2d 1216, 1224 n.1 (10th Cir.), *petition for cert. filed*, 55 U.S.L.W. 3318 (U.S. Sept. 22, 1986) (No. 86-484); *Oreck Corp.* v. *Whirlpool Corp.*, 579 F.2d 126, 131 (2d Cir.), *cert. denied*, 439 U.S. 946 (1978). The cases cited by BEC illustrate this. For example, in *Klor's, Inc.* v. *Broadway-Hale Stores*, 359 U.S. 207 (1959), this Court applied the *per se* rule to a retailer's group boycott claim against a number of major appliance manufacturers and Broadway-Hale, a competing retailer. *Id.* at 212. The Court expressly distinguished the horizontal group boycott present in *Klor's* from a single supplier agreeing to give a single dealer an exclusive dealership agreement. *Id.* at 212-13. Similarly, in *United States* v. *General Motors Corp.*, 384 U.S. 127, 143-45 (1966), this Court found a *per se* illegal horizontal group boycott because a large number of dealers combined to pressure their common supplier not to sell to competing dealers.[12] Both before and after *Monsanto*, lower courts have specifically rejected the application of *Klor's* and *General Motors* to a dealer termination case of the kind here involved. *E.g.*, *Lomar Wholesale Grocery*, 824 F.2d at 590; *Oreck*, 579 F.2d at 131.

Every case in which a supplier terminates a dealer at the behest of another dealer would involve a horizontal group boycott as BEC defines that term. If proof of a price fixing agreement is not necessary to bring such cases within the *per se* rule, every plaintiff would simply say its termination was part of a horizontal group boycott instead of a price fixing conspiracy, and *Monsanto* would mean nothing.

To avoid this semantic gamesmanship, whether a dealer termination is posited as part of a vertical price fixing scheme or as part of a horizontal group boycott, the basic inquiry is the same. That inquiry is whether the *Monsanto* standard for *per se* liability in the vertical context—that there exists evidence of a supplier-dealer agreement to set prices—has been satisfied. Thus, in

12. In any event, under this Court's more recent decisions, it is doubtful even in a truly horizontal case that a *per se* analysis would be appropriate. An investigation of the purpose and market impact of horizontal boycotts is required, and only if the object of the boycott is *per se* illegal is the boycott so treated. *FTC* v. *Indiana Fed'n of Dentists*, 476 U.S. 447, 106 S. Ct. 2009, 2018-19 (1986); *Northwest Wholesale Stationers* v. *Pacific Stationery & Printing*, 472 U.S. 284, 298 (1985).

National Marine Electronic Distributors v. *Raytheon Co.*, 778 F.2d 190, 193 (4th Cir. 1985), where plaintiff also claimed that it was terminated at the behest of competing dealers, the court held:

> [I]n order to conspire to restrain retail price competition there must be some agreement to set, control, fix, maintain, or stabilize prices. . . . [W]hether one chooses to allege that the restraint is vertical or horizontal, the lack of a conspiracy to restrain prices leads to the same result. *Monsanto* bars National's claim.

Accord Lomar Wholesale Grocery, 824 F.2d at 590; *Valley Liquors*, 822 F.2d at 660 n.5 ("The actual label placed on the conspiracy is a 'pedantic distinction,' . . . as the *Monsanto* standard applies regardless of which label is attached.") (citations omitted).

For these reasons, even if BEC's group boycott claim were not infirm for want of timely interposition, it should be rejected for a complete want of merit.

C. Post-*Monsanto* Decisional Law Makes Clear That An Agreement Between A Supplier And A Dealer To Terminate A Competing Dealer Because Of Its Discounting, However Denominated, Is Not *Per Se* Illegal Absent An Agreement On Price

Following *Monsanto*, *every* circuit in its most recent decision considering the issue has adopted the same rule applied by the court below. Each such circuit has held that there must be proof of an agreement to maintain resale prices—not merely an agreement between a supplier and a dealer that is "price related," or "price motivated," or that affects or reduces intrabrand price competition or eliminates a discounter—before there may be a finding of *per se* illegality:

> [A]s post-*Monsanto* authority recognizes, for a terminated dealer to prevail on its per se claim, the evidence must be sufficient for the jury to determine not merely that the manufacturer and nonterminated dealer conspired, but that they conspired to maintain resale prices.

McCabe's Furniture, Inc. v. *La-Z-Boy Chair Co.*, 798 F.2d 323, 329 (8th Cir.), *petition for cert. filed*, 55 U.S.L.W. 3495 (U.S. Dec. 29, 1986) (No. 86-1101). *Accord Lomar Wholesale Grocery*, 824 F.2d at 589; *Valley Liquors*, 822 F.2d at 662; *Garment District, Inc.* v. *Belk Stores Services, Inc.*, 799 F.2d 905, 911 (4th Cir.), *petition for cert. filed*, 55 U.S.L.W. 3476 (U.S. Nov. 17, 1986) (No. 86-794); *Westman Commission Co.* v. *Hobart International, Inc.*, 796 F.2d at 1222-24; *see also O.S.C. Corp.* v. *Apple Computer, Inc.*, 601 F. Supp. 1274, 1293-94 (C.D. Cal. 1985), *aff'd*, 792 F.2d 1464 (9th Cir. 1986); *Reborn Enterprises* v. *Fine Child, Inc.*, 590 F. Supp. 1423, 1439-40 (S.D.N.Y. 1984), *aff'd*, 754 F.2d 1072 (2d Cir. 1985).[13]

Pursuant to *Monsanto*, then, so long as the supplier does not secure an express or implied agreement from the remaining dealer as to the prices it will charge, there is no *per se* illegality.[14]

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13. These decisions dispose of the handful of pre-*Monsanto* cases which BEC claims adopted its theory that an agreement to terminate a discounting dealer constitutes a vertical price fixing agreement. *E.g.*, *Zidell Explorations, Inc.* v. *Conval Int'l, Ltd.*, 719 F.2d 1465 (9th Cir. 1983); *Cernuto, Inc.* v. *United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979), *cited in* BEC Br. at 24-25. *But see Filco* v. *Amana Refrig'n, Inc.*, 709 F.2d 1257 (9th Cir.) (Ninth Circuit rule pre-*Monsanto* required proof of adherence to supplier's prices for vertical price fixing), *cert. dismissed*, 464 U.S. 956 (1983).

The only post-*Monsanto* cases BEC cites are *Jayco Sys.* v. *Savin Bus. Mach.*, 777 F.2d 306 (5th Cir. 1985), *cert. denied*, 107 S. Ct. 73 (1986), a Fifth Circuit decision rendered prior to the decision below, and two decisions from the Eighth Circuit, *Lomar Wholesale Grocery* and *Victorian House, Inc.* v. *Fisher Camuto Corp.*, 769 F.2d 466 (8th Cir. 1985). BEC Br. at 25-26. It is hard to tell what comfort BEC derives from these cases. In affirming summary judgment in favor of the supplier, the *Lomar* court indicated that the pre-*Monsanto* line of authority relied on by BEC was overruled by *Monsanto*, and that *Fisher Camuto* was viable only if it was read to mean that an actual agreement on prices is required to state a claim of *per se* illegality under section 1. *Lomar Wholesale Grocery*, 824 F.2d at 589-90, 592.

14. Subsequent to *Monsanto*, this rule was also adopted by the Antitrust Division of the United States Justice Department in its Vertical Restraints Guidelines. U.S. Dep't Justice, Vertical Restraints Guidelines at 10 (January 23, 1985), *reprinted in* 5 Trade Reg. Rep. (CCH) ¶ 50,473. Indeed, the Antitrust Division read *Monsanto* as requiring evidence of an explicit agreement on prices before a vertical price fixing agreement is established. *Id.*

(footnote continued on following page)

Even if BEC established that Sharp agreed to terminate its dealership because of BEC's discounting, this would not establish that Sharp dictated prices to Hartwell, or that Hartwell adhered to Sharp's prices, or that Hartwell ceded any of his ability to price in accordance with his own business judgment. The court of appeals was therefore correct in holding that the agreement alleged by BEC was not *per se* illegal.

POINT II

AN AGREEMENT BETWEEN A SUPPLIER AND A DEALER TO TERMINATE A DISCOUNTING DEALER FREQUENTLY HAS SIGNIFICANT PRO-COMPETITIVE VALUE AND SHOULD NOT BE SUBJECT TO *PER SE* ILLEGALITY

As shown above, an agreement between a supplier and a dealer to terminate another dealer because of its discounting does not fall within any established category of *per se* restraint. BEC's real complaint is that the court of appeals refused to create a new category of *per se* restraints encompassing such an agreement.

There was no error by the court of appeals in this regard. The normal test for illegality under section 1 of the Sherman Act is

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(footnote continued from previous page)

BEC and its *amici* contend that Congress has criticized the Antitrust Division as attempting to extend the holding of *Monsanto*. BEC Br. at 37-38; NMRI Br. at 12-13; Brief of Amicus Curiae K Mart Corporation in Support of Petitioner at 17-18. Whatever intellectual interest may pertain to this debate between the executive and legislative branches, it need not be resolved in this case. As the United States pointed out in its brief at the certiorari stage:

> [T]he guidelines' definition of the *per se* rule is narrower than the definition adopted by the court of appeals . . . . Congress criticized that narrow rule (see § 605, 99 Stat. 1169); it did not express a view regarding the somewhat broader rule adopted by the court of appeals.

U.S. Br. at 11 n.12.

More to the point, not even BEC or its *amici*, which cite a plethora of Congressional statements and enactments they claim support BEC's position, go so far as to suggest that Congress supports a rule that termination of a free rider, without any proof of an agreement on resale prices, would constitute *per se* illegal price fixing. That, however, is the issue before this Court.

the rule of reason. The *per se* rule is employed only in those limited circumstances where courts have had considerable experience with the challenged conduct, and that experience shows the conduct consistently has a "pernicious effect on competition and lack[s] any redeeming virtue." *Northern Pacific Railway* v. *United States*, 356 U.S. 1, 5 (1958). If a restraint has even any arguable pro-competitive effect, the rule of reason should apply. *Sylvania*, 433 U.S. at 49-50.[15]

BEC's argument to expand the application of the *per se* rule is based on two distinct contentions. First, BEC asserts that because a horizontal agreement between two suppliers to eliminate discount price competition on the sales of their respective products would be *per se* illegal, a like rule is perforce appropriate in the vertical context. BEC Br. at 9, 13-14 n.6, 15, 18-19.[16]

BEC's second argument is that when a supplier agrees to eliminate a discounting dealer, this facilitates a price increase by the remaining dealer. BEC contends that any practice of a supplier that has the purpose or effect of raising its dealer's resale price is on its face pernicious and without redeeming value. BEC Br. at 10; 19-21.

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15. In the decade since *Sylvania* overruled *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), and held all non-price vertical restraints subject to the rule of reason, this Court has consistently limited the scope of the *per se* rule, reaffirming that a market impact approach is the preferred method of analysis under section 1. *E.g.*, *Northwest Wholesale Stationers* v. *Pacific Stationery & Printing*, 472 U.S. 284, 295-98 (1985) (horizontal group boycotts should not automatically be condemned *per se*; examination of market facts required); *Jefferson Parish Hosp. Dist. No. 2* v. *Hyde*, 466 U.S. 2, 26-29 (1984) (tying arrangements not necessarily *per se* illegal); *see also Broadcast Music, Inc.* v. CBS, 441 U.S. 1, 8-9 (1979).

16. Thus, BEC places heavy reliance on *Catalano, Inc.* v. *Target Sales*, 446 U.S. 643 (1980) (per curiam), *cited in* BEC Br. at 9, 16, 18-19, which held that an agreement among beer wholesalers to eliminate short-term trade credit previously granted to beer retailers constituted *per se* illegal price fixing. *Catalano*, 446 U.S. at 648. In so deciding, the Court stated that such "[a] horizontal agreement to fix prices is the archetypical example of [plainly anticompetitive] conduct," *id.* at 647, and further noted that the respondent wholesalers did not even attempt to "suggest a procompetitive justification for a horizontal agreement to fix credit." *Id.* at 646 n.8.

Although BEC proposes a novel *per se* rule, it does so without any supporting economic or legal analysis. Moreover, BEC ignores the extensive discussion of the competitive value of vertical restraints found in *Sylvania*, 433 U.S. at 53-58 and nn.22, 24-26, and *Monsanto*, 465 U.S. at 762-64. BEC ignores as well the wealth of antitrust commentary that specifically addresses whether a supplier-dealer agreement that reduces or eliminates intrabrand price competition should be summarily condemned. These analyses demonstrate that BEC's arguments are specious. Indeed, they conclusively demonstrate that an agreement of the kind BEC alleges has significant pro-competitive value in a wide variety of cases. Moreover, the new *per se* rule BEC proposes is unworkable and unwise. It would eliminate the objective standard of *Monsanto*, would permit a jury to find *per se* liability based upon speculation as to a supplier's motive, and would have a chilling effect on pro-competitive conduct.

A. *Sylvania* Establishes That Vertical Restraints Should Not Be Deemed *Per Se* Illegal Merely Because Similar Restraints Among Horizontal Competitors Are *Per Se* Illegal

BEC's first assertion—that the rule applicable to horizontal agreements to eliminate price competition should also apply in the vertical context—is an antitrust anachronism. The notion that a particular vertical practice should be deemed *per se* illegal just because a like practice among horizontal competitors would be *per se* illegal was appropriately discarded when this Court overruled *Schwinn* in *Sylvania*.

From an antitrust standpoint, horizontal and vertical agreements are fundamentally different creatures. Agreements among suppliers to eliminate price competition on their different brands of products serve no purpose but to limit output and increase prices. By reason of such an arrangement, a supplier can raise its wholesale price and make a higher profit even if it sells less product. While suppliers benefit from this arrangement, consumers pay a higher price and have fewer competing

products among which to choose. It is for this confluence of reasons that such horizontal agreements are condemned as *per se* injurious to competition. *See generally* U.S. Br. at 6-7.

By contrast, a vertical agreement benefits the supplier only if it increases the sales of the supplier's products. The supplier typically receives its payment from the dealer when the dealer makes its purchase from the supplier, not when the dealer resells the product, and the supplier's profit remains the same no matter what resale price the dealer charges. Not only does a supplier derive no benefit from an increase in its dealer's prices, but where there is significant interbrand competition, an artificially high price at the dealer level serves only to boost sales of competing products to the detriment of the supplier. *Sylvania*, 433 U.S. at 56 n.24 ("'Generally a [supplier] would prefer the lowest retail price possible, once its price to dealers has been set, because a lower retail price means increased sales and higher [supplier] revenues.'") (citation omitted); *see generally* R. BORK, THE ANTITRUST PARADOX at 289-91 (1978).

The ordinary, foreseeable and only logical purpose, then, of supplier-dealer agreements is a pro-competitive one, that is, to increase the number of products the dealer buys and resells. For this reason, discussions between vertically aligned parties on prices, output and distribution systems—discussions that might well be deemed *per se* illegal in the horizontal context, *see United States* v. *Container Corp.*, 393 U.S. 333, 337 (1969)—are absolutely necessary. Rather than suppressing such discussions, the antitrust laws encourage them, because they lead to greater product availability to the ultimate consumer. *Monsanto*, 465 U.S. at 764 (to suppress such discussions would "create an irrational dislocation in the market."); *accord Lomar Wholesale Grocery* v. *Dieter's Gourmet Foods*, 824 F.2d 582, 593-94 (8th Cir. 1987); *Illinois Corporate Travel, Inc.* v. *American Airlines*, 806 F.2d 722, 726 (7th Cir. 1986) ("In any chain of distribution discussions of price will be frequent—and as *Monsanto* pointed out, beneficial too."); *see generally* Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 ANTITRUST L.J. 135 (1984).

BEC's attempt to predicate a *per se* rule for the vertical context on a horizontal analogy fails of its own weight.

B. Vertical Restraints Further Pro-Competitive Values Such As The Promotion Of Consumer Services And The Elimination Of Free Riding, And Therefore Should Not Be Deemed *Per Se* Illegal Even If They May Increase Resale Prices

BEC's second contention is that the antitrust laws should condemn agreements to terminate a discounter as *per se* illegal because they may lead to increases in the resale price of the supplier's product. This is another effort by BEC to turn the antitrust clock back to the days of *Schwinn*.

As this Court recognized in *Sylvania*, virtually all vertical restrictions have a tendency to increase prices at the dealer level. If the hallmark of *per se* illegality were the tendency of a restraint to facilitate a dealer price increase, there would be nothing left of *Sylvania* or *Monsanto*. *See, e.g.*, U.S. Br. at 11 ("Treating any reduction in price competition as justifying application of the per se rule would result in the application of the per se rule to virtually all vertical restraints, contrary to this Court's decisions in *Sylvania* and *Monsanto*.")[17]

Sylvania rejected BEC's argument because many vertical restraints simultaneously stimulate interbrand competition. 433 U.S. at 51-52. Often, the only way suppliers can persuade dealers to invest in their products and promote them vigorously against competing brands is if those dealers are able to charge prices that allow them to recapture their investment. *Id.* at 55. As the United States pointed out in this case:

> [T]o the extent that vertical restrictions succeed in encouraging dealer efforts, and thereby strengthen a product's competitive position, they do so precisely because

17. The fact that the *per se* rule against vertical price fixing is not premised upon a concern that prices may increase is shown by this Court's decision in *Albrecht v. Herald Co.*, 390 U.S. 145 (1968), holding that an agreement between a supplier and a dealer to set *maximum* prices is no less illegal than an agreement to set *minimum* prices.

> they allow dealers to charge prices that cover the costs of providing the extra services that the manufacturer deems necessary for the efficient distribution of the product.

U.S. Br. at 10 (footnote omitted). To say that a particular practice may lead to a higher resale price, then, is to say nothing about its purpose or overall effect on interbrand competition, the factors that are critical to determining whether the *per se* rule should apply. *Sylvania*, 433 U.S. at 54-59.

While BEC ignores these factors, courts have considered them in the context of the specific agreement at issue in this case—an agreement to terminate a discounting dealer. The conclusion has been that in most instances the purpose of such an agreement is *not* to permit a dealer to price-gouge—a practice that, as noted, would probably benefit no one and as an economic reality could not benefit the supplier. *See Sylvania*, 433 U.S. at 56 n.24. Rather, such an agreement is typically designed to further a pro-competitive end—the creation or protection of a distribution system that maximizes sales of the supplier's products against competing brands. *Monsanto*, 465 U.S. at 763-64; *Sylvania*, 433 U.S. at 54-56; *see also* Bork, *Vertical Restraints: Schwinn Overruled*, 1977 SUP. CT. REV. 171.

The pro-competitive nature of such an agreement follows from the fact that in many industries there is a need for pre-sale, point-of-sale or post-sale dealer services to stimulate demand for a product. *Sylvania*, 433 U.S. at 53-54. In some instances, the dealers will provide these services of their own accord. In many instances, however, even though these services are necessary to stimulate demand, they will be provided only if they are required by the supplier:

> Because of market imperfections such as the so-called "free rider" effect, these services might not be provided by [dealers] in a purely competitive situation, despite the fact that each [dealer's] benefit would be greater if all provided the services than if none did.

Sylvania, 433 U.S. at 55.

The present case well illustrates this "free rider" effect. One dealer, a Hartwell, appreciates the need for pre-sale promotion, education and other customer services if the supplier's product is to be sold, and he therefore makes the requisite investment in these services. A competing dealer, a BEC, realizes that these efforts will stimulate demand at no cost to it. Since the free rider has none of the full service dealer's selling expenses—no sales-people salaries, advertising or promotional costs—it can undercut the full service dealer's prices and take away the customers he has developed.

In the short run, such free riding means that some customers may be able to obtain a lower price on the supplier's product. In the long run, however, competition and the welfare of consumers suffer. A full service dealer cannot afford to maintain its level of services and meet the discounted free rider price *ad infinitum*. Ultimately, it must eliminate the services it was providing or abandon the market to the free rider. In either case, the pre-sale, point-of-sale and post-sale services necessary to educate the consumer and stimulate sales are lost, to the detriment of the supplier and the consumer alike. Cady, *Reasonable Rules and Rules of Reason: Vertical Restrictions on Distributors*, 46 J. MARKETING 27, 31-32 (1982); Bork, *Vertical Restraints: Schwinn Overruled*, 1977 SUP. CT. REV. at 181.

How to deal with the anticompetitive effects of free riding has become a seminal issue in contemporary antitrust law. Remarkably, but understandably, BEC is all but silent on this issue in its brief. This Court has not been silent, however. To the contrary, *Sylvania* first recognized and "*Monsanto* . . . resoundingly reaffirms the . . . centrality of free-rider concerns in fashioning antitrust rules . . . ." Popofsky & Bomse, *From Sylvania to Monsanto: no longer a "free ride"*, 30 ANTITRUST BULL. 67, 93 (1985).

In order to promote dealer services (which not even BEC asserts are anti-competitive) and to prevent free riding (which not even BEC asserts is pro-competitive), the *Sylvania* and *Monsanto* decisions do two things. First, they recognize that the

supplier is ordinarily in the best position to determine how to market its products efficiently. Thus, they permit the supplier to require that dealers provide the pre-sale, point-of-sale or post-sale services which the supplier believes are necessary to promote the sale of its products. *Sylvania*, 433 U.S. at 55; *Monsanto*, 465 U.S. at 762-64.

Second, these decisions confirm that the supplier may take steps to ensure that dealers will agree to incur the additional costs these services entail. Specifically, the supplier may restrict intrabrand competition for the product, by, for example, providing the dealer with an exclusive territory. *Sylvania*, 433 U.S. at 55; *Monsanto*, 465 U.S. at 762-64.

This reduction in intrabrand competition may enable the dealer to charge a higher price on the supplier's product than if there were several dealers selling the same brand in competition with one another. However, it also provides the dealer with the economic incentive to furnish the services necessary to make the product competitive on an interbrand level. *Sylvania*, 433 U.S. at 54-55; Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6, 11 (1981).

Where the supplier finds that its dealers are not complying with its distribution requirements, it must be free to terminate those dealers. Otherwise, its right to structure a distribution system that maximizes the sale of its products is illusory. Indeed, this was precisely the fact pattern in *Sylvania*. There, the defendant manufacturer prescribed that dealers could only sell television sets from authorized locations. Consequently, each dealer had a territory insulated from intrabrand competition and could recover the costs it incurred in promoting the defendant's product. *Sylvania*, 433 U.S. at 38. When the plaintiff dealer violated the locations clause, its dealership was terminated. *Id.* at

39-40. This Court held that the locations clause, and the plaintiff's termination pursuant to that clause, should be evaluated under the rule of reason. *Id.* at 58-59.[18]

The supplier's general right to terminate dealers who disrupt its distribution system, recognized in *Sylvania*, has special application where the termination arises from the dealer's free riding. In such an instance, the supplier is acting not merely to preserve a distribution system that it views as efficient and pro-competitive, but to prevent a practice that this Court recognized has a corrosive effect on competition:

> The validity and legality of manufacturers' prevention of free riding . . . has been settled by the Supreme Court in *Monsanto* . . . and *Sylvania* . . . .

Local Beauty Supply v. *Lamaur, Inc.*, 787 F.2d 1197, 1202 n.2 (7th Cir. 1986); *see also* Popofsky and Bomse, *From Sylvania to Monsanto: no longer a "free ride"*, 30 ANTITRUST BULL. at 93-94.

Often, as in this case, the impetus for the termination comes from a full service dealer who is upset at the discount prices the free rider can offer by reason of its lower sales costs. *See, e.g., Lomar Wholesale Grocery* v. *Dieter's Gourmet Foods*, 824 F.2d at 593-94; *Garment District, Inc.* v. *Belk Stores Services, Inc.*, 799 F.2d at 909-10. However, no matter where they originate, the concerns are legitimate and the effect of the termination is no different from the supplier's providing another dealer with a protected territory as in *Sylvania*. *See Monsanto*, 465 U.S. at 762. In both instances, the reduction in intrabrand competition enables the remaining dealer to provide the services necessary to stimulate consumer interest and compete more effectively in the interbrand market.[19]

18. On remand, the district court in *Sylvania* held the termination to be lawful under the rule of reason and dismissed the case; the court of appeals affirmed. *Continental T.V., Inc.* v. *GTE Sylvania Inc.*, 461 F. Supp. 1046 (N.D. Cal. 1978), *aff'd*, 694 F.2d 1132 (9th Cir. 1982).

19. In fact, the territorial limitations authorized by *Sylvania* are more restrictive of intrabrand competition than a free rider termination. With a free

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Therefore, while an agreement to terminate a discounting dealer may lead to an increased resale price by the remaining dealer sufficient to cover the cost of necessary dealer-provided services, that is a pro-competitive effect, of benefit to suppliers and consumers alike. It is most unlikely to be the product of an anticompetitive motive by the supplier.

In addition, by reason of built-in checks in the marketplace, such an agreement is most unlikely to have any unreasonable effect on competition. In a market as competitive as electronic calculators, interbrand competition provides a strict check on the prices that even a full service dealer may charge. *See, e.g., Sylvania*, 433 U.S. at 52 n.19, 54. Finally, absent an agreement on prices, the full service dealer is still free to adjust its resale price as competitive circumstances dictate by, for example, discounting where necessary to make a particular sale if, in the dealer's independent judgment, such a course is desirable. *See, e.g., National Marine Electronic Distributors* v. *Raytheon Co.*, 778 F.2d 190, 193 (4th Cir. 1985) ("Raytheon did not require its dealers to sell at any fixed price. The dealers set their own retail prices, each taking into consideration its own cost of goods, overhead expenses, and a profit margin that was as much as the market would bear considering demand and competition.").

For these reasons, as the United States summed up at the certiorari stage in this case (U.S. Br. at 12):

> [A] vertical agreement to restrict intrabrand price competition by eliminating a discounting dealer—without prescribing the level of the remaining dealer's resale prices—may "'increase economic efficiency and render markets more, rather than less, competitive.'" *Northwest Wholesale Stationers, Inc.*, 472 U.S. at 295, quoting *Broadcast Music, Inc.*, 441 U.S. at 20. Such a restraint is therefore properly evaluated under the rule of reason.

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rider termination, other dealers selling the supplier's product can still compete with the remaining dealer. When the supplier grants a protected exclusive territory, *all* intrabrand competition is eliminated.

C. To Subject A Supplier To *Per Se* Liability For Terminating A Free Riding Dealer Would Create An Irrational Dislocation In The Marketplace Of The Kind Warned Against In *Monsanto*

Perhaps the most troubling aspect of BEC's proposed new *per se* rule is the damage it would cause in the marketplace. Antitrust rules do not exist divorced from practical realities, *Sylvania*, 433 U.S. at 47, and, practically speaking, BEC's new *per se* rule makes no real world sense.

For example, BEC conveniently ignores the fact that its proposed rule of *per se* illegality would straightjacket the supplier who finds himself the unwelcome recipient of an "it's him or me" ultimatum. Just as complaints by a dealer to its supplier about another dealer's discount pricing are a normal and, from the supplier's standpoint, an unavoidable fact of life in the marketplace, *Monsanto*, 465 U.S. at 763, where a full service dealer is faced with a free rider problem, not only complaints, but ultimata of this kind are inevitable. *See, e.g., Belk Stores*, 799 F.2d at 910; *Raytheon*, 778 F.2d at 192.

BEC offers no suggestion as to what the rational supplier is supposed to do when faced with such an ultimatum. As the instant case illustrates, under BEC's rule, by terminating the free rider, even where necessary to avoid the interruption of an efficient distribution system which requires promotion and services, the supplier has placed itself in a position of enormous antitrust vulnerability.

If, however, the supplier ignores the ultimatum, and the full service dealer makes good on its threat and abandons the market to the free rider, the supplier's distribution system falls apart. No one will provide the promotional and educational services necessary to stimulate sales, to the detriment of both the supplier and the consumer. *Isaksen* v. *Vermont Castings, Inc.*, 825 F.2d 1158, 1161 (7th Cir. 1987). *See generally* Popofsky & Bomse, *From Sylvania to Monsanto: no longer a "free ride"*, 30 ANTITRUST BULL. at 89. There is no practical utility in a rule that requires a supplier to sacrifice its best dealers to protect a free

rider. *Belk Stores*, 799 F.2d at 909-10. But that is precisely the rule that BEC proposes.[20]

D. BEC's Attempt to Distinguish This Case From the *Sylvania/Monsanto* Model On The Basis Of Sharp's Alleged Motive In Terminating BEC Highlights The Improvidence Of The New *Per Se* Rule That BEC Advocates

Although the record establishes that Sharp's conduct was the functional equivalent of its providing Hartwell with an exclusive dealership, BEC maintains that this case is distinguishable from the *Sylvania/Monsanto* model. BEC asserts that Sharp terminated BEC not because it wanted to provide Hartwell with an exclusive territory, and not because of BEC's free riding, but in furtherance of Hartwell's desire to eliminate BEC as a discounting rival. *E.g.*, BEC Br. at 7, 10-11. This, BEC argues, evidences the kind of naked anticompetitive conduct that should not be protected under a *Sylvania/Monsanto* analysis. BEC Br. at 22-24.

BEC's argument finds no support in the record. *See infra* p. 38. Even if it did, the argument would have no relevance to the question of whether a new *per se* rule is required. "*Per se* rules . . . require the Court to make broad generalizations about the social utility of particular commercial practices" and are not created to address one particular case. *Sylvania*, 433 U.S. at 50 n.16; *see also Lomar Wholesale Grocery*, 824 F.2d at 591. However, BEC's motive argument does serve a useful purpose. It

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20. Indeed, the court in *Belk Stores*, 799 F.2d at 908, concluded that where a supplier terminates a discounter in response to an ultimatum from a better dealer, there is no agreement at all within the meaning of *United States* v. *Colgate & Co.*, 250 U.S. 300 (1919). In such circumstances, the supplier is not "agreeing" to do anything. It is simply sacrificing one customer in order to retain a better customer. Such an action is in the independent self-interest of the supplier. Consistent with *Monsanto*, it fails to give rise to any section 1 claim. *Belk Stores*, 799 F.2d at 911. *See also Oreck Corp.* v. *Whirlpool Corp.*, 579 F.2d 126, 131 n.6 (2d Cir.) (ultimatum cases should be evaluated under the rule of reason), *cert. denied*, 439 U.S. 946 (1978).

further highlights the improvidence of the new *per se* rule that BEC advocates.

The reason any supplier adopts a system of restricted distribution—be it a territorial restraint, an exclusive dealership, or some other formulation—is to reduce intrabrand price competition so that its dealers can focus on competing against other suppliers' brands:

> The adoption of a restricted distribution system implies a decision to emphasize nonprice competition over price competition, which such a system tends to suppress.

Valley Liquors, Inc. v. *Renfield Importers, Ltd.*, 678 F.2d 742, 743-44 (7th Cir. 1982).

To ask a jury whether the supplier's motive in refusing to deal with a particular customer was a desire to reduce price competition or a desire to promote a system that has the necessary effect of reducing price competition, and to have *per se* illegality hinge upon this semantic distinction, is a tenuous basis for a rational system of antitrust jurisprudence in any context. In the free rider context, permitting a jury to attempt to draw such a distinction makes even less sense. By definition, a free rider competes on the basis of the discount prices its lower sales costs enable it to charge. While not all discounters are free riders, all free riders are discounters. *Beach* v. *Viking Sewing Machine Co.*, 784 F.2d 746, 751 n.6 (6th Cir. 1986); *see generally* Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6, 12-13 (1981). When a full service dealer complains about a free rider, it is complaining about the free rider's discounting. *See, e.g., Isaksen* v. *Vermont Castings, Inc.*, 825 F.2d 1158, 1161-62 (7th Cir. 1987); *National Marine Electronic Distributors, Inc.* v. *Raytheon Co.*, 778 F.2d 190, 191 (4th Cir. 1985). Concomitantly, when a supplier agrees to terminate a free rider to stop its free riding, a supplier is agreeing to terminate a discounter to stop its discount price competition.

The policies of *Sylvania* and *Monsanto* would be frustrated by a rule that permits the jury to speculate as to whether a supplier

terminated a free rider because of free riding or because of discounting. Rather than risk treble damage liability because of the possibility that a jury might conclude that its efforts to deter free riding and promote an efficient distribution system were motivated by an antipathy toward intrabrand price competition, a supplier would simply forego requiring the kind of promotional and educational services that benefit the marketplace as a whole.

This is not an academic concern. The marketplace does not run by itself. Each day a supplier must make a myriad of decisions regarding marketing practices generally and its distribution system specifically. No matter how attractive the Sharp product, if Sharp does not have an effective distribution system that product will sit on the warehouse floor. An inefficient distribution system benefits no one, and once a supplier realizes a particular dealer is inappropriate, undue delay in correcting the situation is costly.

Many suppliers have literally thousands of dealers or distributors throughout the United States and each day face questions of whom to appoint, whom to terminate and when to terminate in order to build a more efficient, competitive distribution system. Suppliers cannot do this if the antitrust laws treat every dealer termination as a near occasion to treble damage liability, or force them to guess at their peril as to how a jury, unchecked by any objective criteria, will perceive their motives in making these changes.

To ensure that the antitrust laws do not have the anomalous effect of chilling the very conduct authorized by *Sylvania*, the objective rule prescribed by *Monsanto*—whatever the motivation for the termination, did the supplier and the remaining dealer actually agree to fix prices—is far preferable. As Judge Posner recently stated for the court in *Morrison* v. *Murray Biscuit Co.*, 797 F.2d 1430, 1440 (7th Cir. 1986), citing with approval the decision of the court of appeals in this case: "[A]ntitrust liability should not turn on a court's guess as to which motive may have predominated."

Finally, although BEC speaks in terms of motives, it also appears that BEC is suggesting that promotional, educational or other dealer services were not necessary in this case, and that Sharp's actions had an adverse effect on competition. *See, e.g.*, BEC Br. at 31. If this is BEC's argument, it suffices to say that BEC is simply wrong. The record affirmatively establishes that Sharp's conduct was both reasonable and pro-competitive.

In 1973 the electronic calculator industry involved a new product that was complex and expensive. This structure necessitated promotion, education and other dealer level services if demand was to be stimulated. Tr. 113-14; 343-48; 1429-32. This structure also invited free riding, *see generally Isaksen* v. *Vermont Castings, Inc.*, 825 F.2d 1158, 1161-62 (7th Cir. 1987), and the record makes clear that BEC was in fact free riding on Hartwell's sales efforts. Tr. 110; 279-80; 283-84; 343-44; 346-48; Pet. App. at 20a (Jones, J., concurring).

The record also shows that, consistent with the *Sylvania/Monsanto* model, Sharp's actions were not injurious to competition:

> Only atavistic devotees of the abacus or slide rule could fail to recall the remarkable history of the electronic calculator market during the last fifteen years. The range of available models, variety of functions that can be performed, and myriad optional enhancements have multiplied rapidly while the average prices have plummeted. The number of competing manufacturers has increased. To maintain their market position and profitability, manufacturers like Sharp have obviously been required to react quickly and imaginatively to changes in the marketplace. The record in this case reveals that both Sharp's market share and the retail prices of its calculators were declining in this period.

Pet. App. at 19a-20a (Jones, J., concurring) (footnote omitted).

Thus, whether considered in terms of broad generalities or on the specific facts of this case, there is no basis to assume that where a supplier agrees to terminate a discounting dealer, it has an anticompetitive purpose, nor any reason to believe that the

effect of the termination—even if it results in a higher price at the dealer level—is without redeeming competitive value. Accordingly, the conclusion of the court of appeals that an agreement to terminate a discounting dealer—absent evidence of actual price fixing—should not be subject to condemnation by a *per se* rule should be affirmed.

POINT III
ALL VERTICAL RESTRAINTS SHOULD BE EVALUATED UNDER THE RULE OF REASON

The same reasons leading to the conclusion that vertical nonprice restraints are subject to the rule of reason support the conclusion that vertical price restraints should also be subject to the rule of reason.

BEC maintains that the issue of how to treat vertical price fixing is not before the Court. BEC Br. at 36 n.11. However, while Sharp's cross-petition—which asked the Court to hold vertical price fixing subject to the rule of reason and to order dismissal of the case—is still pending, much of BEC's brief, and the briefs of its *amici*, are devoted to the proposition that the rule holding resale price maintenance *per se* illegal should not be disturbed. Their arguments deserve a brief response.[21]

A. There Is No Economic Justification For The Application Of The *Per Se* Rule To Vertical Price Restraints

The *per se* rule applicable to resale price maintenance has not been re-examined by this Court since it was adopted some 75

21. Even if BEC had not injected this issue into the case, it still would be properly before the Court since a determination that resale price maintenance is subject to the rule of reason constitutes an alternative basis for affirmance. The judgment below was a reversal and remand for a new trial. A determination that the *per se* rule no longer applies may well permit BEC to re-try the case on a rule of reason theory in light of the change in law. *Cf. Sylvania*. Accordingly, a finding that resale price maintenance is no longer subject to the *per se* rule would not alter or enlarge the relief granted below and thus may be heard at this time. *Blum* v. *Bacon*, 457 U.S. 132, 137 n.5 (1982); *see generally* R. STERN, E. GRESSMAN & S. SHAPIRO, SUPREME COURT PRACTICE § 6.35, at 382 (6th ed. 1986).

years ago in *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U.S. 373 (1911). Consistent with the traditional analysis applied by this Court, the *per se* rule can be justified only if there is some basis for concluding that resale price maintenance is in fact inimical to the goals of the Sherman Act. *Sylvania*, 433 U.S. at 49-50, 50 n.16, 52-53.

The holding in *Sylvania* that vertical non-price restraints are subject to the rule of reason calls into question the continued vitality of applying the *per se* rule to vertical price restraints. *Sylvania*, 433 U.S. at 70 (White, J., concurring). Accordingly, in *Monsanto* the United States asked the Court to review this issue precisely because:

> Such an analysis would show that resale price maintenance, like the nonprice vertical restrictions in *Sylvania*, can have significant procompetitive effects.

Brief for the United States as Amicus Curiae in Support of Petitioner on Writ of Certiorari at 21, *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984) (hereinafter cited as "U.S. Br. in *Monsanto*").[22]

Leading commentators also have emphasized that the *per se* prohibition on resale price maintenance has little legitimacy in light of the principles set forth in *Sylvania*. *E.g.*, Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6, 9 (1981) ("[A]ny free-rider or other arguments that are available to justify exclusive territories are equally available to justify resale price maintenance."); *accord* Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 ANTITRUST L.J. 135, 171 (1984); Baker, *Interconnected Problems of Doctrine and Economics in the Section One Labyrinth: Is Sylvania a Way Out?*, 67 VA. L. REV. 1457, 1465-67 (1981); Bork, *Vertical Restraints: Schwinn Overruled*, 1977 SUP. CT. REV. 171, 181-82. This view has

22. The Court did not reach the issue in *Monsanto* because it was not raised by the parties below. 465 U.S. at 761 n.7. Here, there is no dispute that Sharp properly preserved this issue. *See* Tr. 1584-87; 1594-95; 1598-99; Defendant's Requested Jury Instruction Nos. 23 and 26.

recently been echoed in judicial opinions as well. *E.g.*, *Isaksen* v. *Vermont Castings, Inc.*, 825 F. 2d 1158, 1161-62 (7th Cir. 1987); Pet. App. at 22a-23a (Jones, J., concurring).

While vertical price restraints can be used to achieve all the competitive advantages that vertical non-price restraints achieve—the securing of efficient dealers, providing the impetus to those dealers to furnish pre-sale, point-of-sale or post-sale promotional and educational services and deterring free riding—they present no greater competitive threat than do non-price restraints.

A supplier is unlikely to use a vertical price fixing agreement merely as a way to raise resale prices. If for some reason that were a supplier's goal, it could achieve that goal by any number of infinitely simpler, safer and more effective means. The supplier could raise its price to the dealers so that the dealers would have to raise their resale prices to realize a profit; the supplier could transfer to its dealers on a bona fide consignment basis and legally control their resale prices; or the supplier could do away with a dealership network altogether, vertically integrate, and sell to end users directly via employees or indirectly via independent sales agents, charging whatever price the supplier wants. None of these activities would implicate, much less violate, section 1 of the Sherman Act. *Ryko Manufacturing Co.* v. *Eden Services*, 823 F. 2d 1215, 1222-23 (8th Cir. 1987); *see generally* Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 ANTITRUST L.J. at 143-48.

The supposition that given the power to fix resale prices a supplier would set an excessively high price is an economic makeweight. The supplier's price to the dealer is not affected by the dealer's resale price. Any excessive profit realized from the resale goes into the dealer's pocket. The only rational motivation for a supplier is to fix resale prices at the lowest level necessary to ensure that the dealer can provide necessary promotional and

other customer services. As Judge Posner explained in *Isaksen*, 825 F.2d at 1161:

> If the floor were set higher than necessary to induce dealers to provide the point-of-sale services that would maximize the sales of [the manufacturer's] stoves, [the manufacturer] not only would be transferring wealth from itself to its dealers (and why would it want to do that?) but would be pricing its stoves out of the market. . . .

Therefore, rather than endeavoring to effect an economically senseless price gouge, a manufacturer who employs resale price maintenance usually will be attempting to provide an incentive to its dealers to handle its product in a way that the manufacturer expects will be advantageous in interbrand competition. In other words, it will be using a vertical restraint to increase the sales of its product at the expense of competing suppliers. That is not a pernicious end. It is exactly what suppliers should be doing in a competitive market. There is no need for the antitrust laws to discourage such conduct, and every reason for these laws to encourage it. Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86, 89-96 (1960); R. POSNER, ANTITRUST LAW, AN ECONOMIC PERSPECTIVE at 148-49 (1976).

Accordingly, no economic justification exists for continuing the *per se* prohibition on vertical price fixing.

B. There Are Substantial Economic And Practical Justifications For The Application Of The Rule Of Reason To Vertical Price Restraints

The economic and practical justifications for changing the prohibition are many. In numerous circumstances, resale price maintenance can actually promote competition more effectively than non-price restraints. In some cases, it will be the only way to ensure that dealers provide the requisite pre-sale, point-of-sale or post-sale services needed to stimulate demand and benefit the consumer. While BEC's free riding was ameliorable by Sharp's granting Hartwell the equivalent of an exclusive territory, in

other circumstances this would not have solved the problem.[23] Where dealers must be close together geographically, an exclusive territory is no remedy at all. A resale price fixing agreement "may be the only feasible method [of limiting intrabrand competition among dealers] where effective retail distribution requires that dealers be located close to one another. . . ." Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. at 9.

Where, unlike the instant case, a resale price fixing agreement would constitute the only realistic way of preventing free riding, the sole option available under present law is for the supplier to suffer the free riding, however damaging that might be to its distribution network or to the marketplace generally. It is far preferable to permit the supplier to insist on a fixed price high enough to cover the full service dealer's costs.

Taking account of exactly these factors, the United States has held firm to the view that vertical price fixing is not merely a neutral, but frequently a pro-competitive, device. Although appropriation legislation prohibited the United States from supporting Sharp's cross-petition, *see* U.S. Br. at 15, the head of the Antitrust Division of the United States Department of Justice recently testified before Congress that the Government's views expressed in *Monsanto* have not changed:

> The Department of Justice filed a brief as *amicus curiae* in the *Monsanto* case expressing serious doubts as to the continued legitimacy of the current *per se* rule. We invited the Supreme Court to re-examine the rule, urging that resale price maintenance usually will not be used by the manufacturer simply to increase the retail price of its product, since it can do that more directly by raising its wholesale price. Rather, resale price maintenance usually will be designed to promote interbrand competition by

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23. In fact, the free rider effect, which was a principal reason relied on by the *Sylvania* Court for treating restricted distribution under the rule of reason, was originally presented as a justification for vertical price fixing agreements, not as a justification for territorial or other non-price vertical restraints. *See* Telser, *Why Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86 (1960).

encouraging dealers, *inter alia*, to train sellers, to undertake effective sales promotions, to create attractive showrooms, and to support informational, maintenance or repair services. Resale price maintenance curtails "free rider" dealers, who sell at discount prices to customers attracted to a product by other dealers' advertising or other promotional activities and who thus thwart procompetitive efforts desired by the manufacturer. Economists have posited several other procompetitive explanations of resale price maintenance as well.

. . . .

For the reasons articulated in our *Monsanto* brief, we view resale price maintenance agreements as potentially procompetitive—not just competitively neutral—in many circumstances.

Statement of Charles F. Rule, Acting Assistant Attorney General, Before the Subcommittee on Antitrust, Monopoly and Business Rights of the Senate Judiciary Committee at 6-7 (Apr. 23, 1987); *see also* Address of D. Oliver to the Antitrust Law Section of the American Bar Association (Aug. 12, 1986), *reprinted in* 5 Trade Reg. Rep. (CCH) ¶ 50,481, at 56,287-88.[24]

C. There Is No Congressional Impediment To This Court's Application Of The Rule Of Reason To Vertical Price Restraints

BEC points out that there has been much legislation in the section 1 area and contends that Congress has, by implication, codified the *per se* rule against vertical price fixing. BEC also

24. Undoubtedly, in some circumstances vertical price restraints would not be pro-competitive. If it could be shown that such restraints were being used to foster a supplier or dealer level cartel, that practice would likely fall within categories of *per se* condemnation applicable to horizontal arrangements. Even if the horizontal element went undetected, such practices would still be subject to condemnation under a rule of reason analysis. But to perpetuate a *per se* rule that time has taught to be counterproductive on the ground that circumstances could be hypothesized in which a finding of illegality would make sense violates the basic tenets underlying the *per se* rule. *See* U.S. Br. in *Monsanto* at 7.

suggests that Congress is better equipped than the Court to determine what is and is not *per se* illegal in the vertical context. BEC Br. at 36-38, 38 n.12, 40 n.14, 41-42.

The short answer to BEC's argument that Congress, not the Court, is the appropriate arbiter of *per se* rules is that this argument was made—and soundly rejected—in *Sylvania*. There, this Court reaffirmed that the evaluation of the *per se* rule, particularly in the context of vertical restraints, is the proper office of the judiciary. *Sylvania*, 433 U.S. at 57 n.27.

With respect to its companion argument that Congress has in fact spoken by implication on this point, BEC ignores one rather salient fact. BEC fails to mention that, in the wake of *Monsanto*, legislation was proposed that would explicitly codify the *per se* rule in this context. S. 430, 100th Cong., 1st Sess., 133 Cong. Rec. 1484 (1987); H.R. 585, 100th Cong., 1st Sess. (1987). However, Congress has never enacted that legislation.[25]

In sum, it is well-settled with respect to the Sherman Act that Congress intended the courts to "give shape to the statute's broad mandate by drawing on common-law tradition." *National Society of Professional Engineers* v. *United States*, 435 U.S. 679, 688 (1978); *accord Associated General Contractors, Inc.* v. *California State Council of Carpenters*, 459 U.S. 519, 530-32 (1983). This Court has a special responsibility to revisit and reconsider the application of the Sherman Act as circumstances warrant. This is not an ordinary case of statutory construction where deference to the legislature (and legislative inactivity) is warranted. The Sherman Act is basically a court-made rule, and therefore can and should be changed by the courts—in particular this Court—when it proves unwise or economically counterproductive as in this case. BEC presents no basis whatsoever for this Court to retreat from its traditional role of determining when and to what extent the *per se* rule should be applied. *See Sylvania*, 433

25. The repeal of the fair trade laws, relied upon by BEC as "evidence" of Congressional intent in this regard, BEC Br. at 40 n.14, and other issues of legislative history germane to BEC's argument, were addressed at length by the United States in *Monsanto*. *See* U.S. Br. in *Monsanto* at 27-28.

U.S. at 57 n.27; *United States* v. *Associated Press*, 52 F. Supp. 362, 370 (S.D.N.Y. 1943), *aff'd*, 326 U.S. 1 (1945).

D. This Case Perfectly Illustrates Why Vertical Price Restraints Should Be Evaluated Under The Rule Of Reason

Not only is there good reason for the Court to review and revise the *per se* rule applicable to vertical price restraints, but there is good reason to do so now. As this Court stated in *Sylvania*, 433 U.S. at 51-52, 57-59, too broad an application of the *per se* rule in the vertical context is dangerous because it deters practices that are actually beneficial to competition. The *per se* rule against vertical price fixing should not be continued simply on the basis that it has been in place for a long time, particularly where experience teaches that the rule is harmful to the marketplace as a whole.

And harmful that rule is. This Court has recognized that vertical price restraints are frequently indistinguishable—both in form and effect—from non-price restraints. *Monsanto*, 465 U.S. at 762. Continuing to treat vertical price restraints as *per se* illegal, while acknowledging that in form and effect they are generally indistinguishable from other, presumptively legal, vertical restraints is not only anomalous, *see* Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 ANTITRUST L.J. at 171, and not only ensures an ever swelling volume of lawsuits by terminated dealers, *see* Pet. App. at 21a-22a,[26] but also presents the precise danger of interdicting pro-competitive conduct warned of in *Monsanto*. 465 U.S. at 764.

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26. Judge Jones, concurring below, expressed with admirable clarity the reality of this problem:

> Most clever attorneys, like plaintiff's counsel in this case, will be able to generate sufficient evidence, even pursuant to the *Monsanto* standard, to withstand summary judgment review, and thus to exert substantial influence toward settlement of cases where no anticompetitive harm, or harm to the consuming public, really occurred.

Pet. App. at 21a-22a.

As post-*Monsanto* decisional law establishes, efforts to alleviate the anticompetitive effects of the *per se* rule in the vertical context by strengthening the standards of proof or tightening the definition of price fixing are unavailing. Terminated dealers will continue to challenge terminations as products of price fixing agreements, and the monumental costs and burdens of such suits will necessarily deter suppliers from adopting distribution methods that could otherwise be beneficial both to themselves and to interbrand competition. *See* Pet. App. at 21a-22a (Jones, J. concurring).

This is well illustrated by the instant case. While the court of appeals adopted a carefully focused definition of vertical price fixing, it did not dismiss the complaint against Sharp. Rather, it remanded the case for a new trial on the basis that Hartwell's general adherence to Sharp's suggested resale prices permitted an inference of a price fixing agreement, even though Hartwell testified that his pricing was always the product of independent judgment and not the product of coercion by Sharp. Tr. 294; 327; 332; 333.[27] However, the natural effect of any intrabrand vertical restraint is to impose costs upon a dealer that will necessitate its raising resale prices. In any vertical restraint case, therefore, the predicate for finding an agreement that somehow affects price will exist, even under the court of appeals' standard.

The record in this case shows that interbrand competition in the electronic calculator market was not only fierce at the time of the events in question, but actually *increased* subsequent to the termination of BEC, and has resulted in a reduction in prices and an improvement in the quality and number of products available.

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27. It should be noted that the standard for a permissible inference of price fixing enunciated by the court of appeals falls far short of the *Monsanto* standard. In *Monsanto*, 465 U.S. at 764 n.9, the Court made clear that a price fixing agreement cannot be inferred merely from the dealer's adherence to the supplier's suggested price, but also requires evidence that the dealer communicated its acquiescence to the supplier and that this was sought by the supplier.

Tr. 893-94; 931; 1024; 1027-28. For that reason, Judge Jones stated below:

> I believe this case perfectly illustrates the arguments why vertical price restraints should be tested under antitrust's Rule of Reason rather than, as *Monsanto* continues to require, per se illegality. There is no social benefit to subjecting manufacturers' pricing relationships with their distributors to potential per se illegality where they operate in markets whose interbrand competitiveness overwhelms any detrimental effects of those relationships. And, although *Monsanto* moves toward alleviating the threat of unwarranted treble-damage actions, the abiding uncertainty suggests that the Supreme Court would more wisely jettison the precedent that led to the rule of per se illegality for vertical price restraints.

Pet. App. at 19a (footnote omitted).

This Court admonished in *Matsushita Electric Industrial Co.* v. *Zenith Radio Corp.*, 475 U.S. 574, 106 S. Ct. 1348, 1356 (1986), that the range of permissible inferences under the antitrust laws is limited, and that permitting illogical inferences to be drawn from proven facts could deter the kind of competitive behavior the antitrust laws are designed to promote. It is illogical, if not irrational, to presume conclusively that vertical price fixing is *per se* injurious to competition where conduct indistinguishable in economic effect is regularly regarded as affirmatively pro-competitive. The rule that compels such a presumption should be rejected by this Court.

CONCLUSION

For the foregoing reasons, Respondent Sharp Electronics Corporation respectfully requests that this Court affirm the judgment of the court of appeals.

Dated: New York, New York
November 6, 1987

Respectfully submitted,

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NO. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

REPLY BRIEF OF PETITIONER BUSINESS ELECTRONICS CORPORATION

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MOTION OF PETITIONER FOR LEAVE TO FILE REPLY BRIEF

Respondent's brief on the merits was filed on or about November 6, 1987. Later in November, counsel for petitioner contacted the deputy clerk of the Supreme Court in charge of filing in this case to confirm that petitioner could file a reply brief so long as it was received by the Clerk's office one week prior to oral argument, or by January 12, 1988. On December 8, 1987, the Court amended Rule 35.3 to require, *inter alia,* receipt of a reply brief within

thirty days of the date of the order amending that rule, or by January 8, 1988.

Counsel for petitioner first learned of this amendment on the afternoon of January 7, 1988, during a conversation with the deputy clerk about another matter. Counsel for petitioner had no notice of the Court's amendment to Rule 35.3 from the Clerk's office or otherwise. Under these circumstances, petitioner respectfully requests leave of the Court to file its reply brief on January 12, 1988.

Respectfully submitted,

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NO. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

REPLY BRIEF OF PETITIONER BUSINESS ELECTRONICS CORPORATION

I. Sharp Misstates the Issue and Presents a Repudiated Version of the Facts.

Sharp's Statement of the Case bears little resemblance to the case actually before this Court. According to Sharp, it terminated BEC solely because of poor performance. Sharp made the very same contentions to the jury, *see* Tr. 1525-35, 1543, which found instead that Sharp terminated BEC pursuant to an agreement with Hartwell

to eliminate price cutting. Tr. 1587, J.A. 18-19. Sharp has not appealed the sufficiency of the evidence supporting this finding.[1]

Nevertheless, altering the Question Presented to fit its repudiated version of the facts, Sharp poses the issue as whether "an agreement between a supplier and a full service dealer to terminate a free riding discounter . . . [should] be deemed a form of price fixing unlawful per se." This rendering unfairly loads the question and omits the essential ingredient of the jury's finding: an agreement to eliminate price cutting. This case concerns more than mere termination of a dealer who *happened* to be a discounter. Rather, the Court will decide whether resale price maintenance encompasses an agreement to eliminate price cutting by terminating the price cutter.

A. The "Free Rider" Canard.

Sharp repeatedly characterizes BEC as a "free rider" who did nothing more to promote sales than mail out discount flyers to customers developed at Hartwell's expense and lazily wait for orders to arrive. The evidence simply does not bear out this version of events. *See Business Electronics v. Sharp Electronics Corp.*, 780 F.2d 1212, 1219 (5th Cir. 1986) ("BEC produced evidence tending to show that it was not free riding. . . .").

If anyone "free rode" on another's efforts, Hartwell did. When BEC opened its Sharp dealership in 1968, the Sharp brand was virtually unknown in Houston. During

1. All evidence inconsistent with the jury verdict must be assumed to have been rejected by the jury. See, e.g., Branti v. Finkel, 445 U.S. 507, 512, n.6 (1980). Even if evidentiary sufficiency were at issue, Sharp's Statement of the Case violates the rule that the evidence and reasonable inferences on review are to be construed in favor of the jury's decision. See Continental Ore Co. v. Union Carbide & Carbon Corp., 370 U.S. 690, 696 (1962).

the next four years, BEC devoted considerable effort and expense to develop Sharp business. Tr. 86-88. When Sharp added Hartwell as a dealer in 1982, Hartwell immediately asked for a list of BEC's accounts and tried to buy a customer list from a former BEC salesman. Tr. 445, 1474-75. Hartwell then called on BEC's customers. Tr. 88. Thus, far from "free riding" on Hartwell's sales efforts, BEC competed to prevent Hartwell from taking accounts already developed by BEC.

Neither does the record support Sharp's assertion that BEC "dispensed with its entire sales force, stopped advertising, and let Hartwell's sales people educate prospective customers at Hartwell's expense." Sharp Br. at 5.[2] Ehrenberger personally called on customers and made calculator demonstrations. Tr. 347. Sharp ignores Hartwell's testimony that Ehrensberger was "the most professional calculator salesman [Hartwell] had ever seen," that Ehrensberger was a "formidable opponent," and that he was "good at what he did". Tr. 397, 274, 440. BEC's requirement of fewer salesmen than Hartwell and fewer visits per customer to make a sale hardly made BEC a "free rider."

BEC did not stop advertising and begin discounting when Hartwell became a Sharp dealer. In fact, BEC used sales flyers—a form of advertising—throughout his tenure as a Sharp dealer. Tr. 87-88; *see also* Tr. 837 (Hartwell complained about BEC's "*advertising* of prices at much lower than normal") (emphasis added). Although Sharp

2. Hartwell's testimony that he did not "see" BEC salesmen in the marketplace other than Ehrensberger himself, Tr. 346-48, obviously falls short of proving that BEC in fact had no other salesmen. Sharp cites Tr. 110, where Ehrensberger testified that BEC was down to only a few personnel by June 1973, but Sharp omits any reference to Tr. 111, where Ehrensberger explained that he was referring to the period *after* Sharp cancelled BEC.

states that Hartwell "advertised the Sharp product extensively," Sharp Br. at 5, there is no evidence that Hartwell advertised Sharp products at all during the time in question. Hartwell testified only about his advertising budget in 1981 and 1982 for his entire business, which included many products other than calculators. Tr. 1031. That advertising occurred *nine years* after BEC was terminated.

In short, BEC did what competitors are supposed to do — operate efficiently, use effective salesmanship, and offer competitive prices. The jury was not fooled by Sharp's "free rider" smokescreen, and this Court should not be either.

B. The Quota Excuse.

The record also contradicts Sharp's contention that "Hartwell's performance [was] generally . . . superior [to BEC's]". Sharp Br. at 6. Sharp fails to mention that BEC's sales suffered because Sharp withheld delivery of preferred calculator models as discipline for BEC's continued price cutting. *See* Tr. 77-80.[3] Despite these difficulties, BEC's sales and quota achievement record was virtually identical to Hartwell's during the one year they competed. PX 110, Tr. 1163-64, 1358. Furthermore, the record contains ample other evidence from which the jury could reasonably find that quota achievement had little, if anything, to do with BEC's termination. Sharp did not complain to BEC about quota achievement, only about pricing. Tr. 1414. Indeed, when Hartwell was first asked about Sharp's quotas at trial, he laughed. Tr. 301. Sharp's representative, too, testified that the quota levels were often arbitrary and almost a joke. Tr. 604-605, 616-17.

3. Sharp's representative told Ehrensberger that Sharp was in a position to make inventory problems very "painful" for BEC if it continued to price "arbitrarily." *Id.*

C. The True Reason for BEC's Termination: An Agreement to Eliminate Price Cutting.

According to Sharp, neither it nor Hartwell really cared about the price charged by BEC so long as BEC did not "free ride" on Hartwell's sales effort. The jury did not believe this theory, and the evidence belies it. In reality, Hartwell invited BEC to participate in a classic horizontal price-fixing conspiracy:

> One of my salesmen called on Delmar Petroleum Company. . . . At my suggestion, my salesman backed off and *we will not compete on this deal with you*. I particularly wanted to point out to you that we are making the first step on backing off so the customer won't be able to play one of us against the other in a *"discount" situation*.

PX 40 (emphasis added); Tr. 84-86. Regarding this letter, Hartwell testified that " 'discount' situation" meant:

> I was making the first step to lending some *price stability*, I guess you would say, to Mr. Ehrensberger. . . . Meaning that I was going to sell my product at the manufactured [sic] suggested list. That it was up to him what he wanted to sell it at.

Tr. 276-77 (emphasis added). Hartwell wanted to "avoid" BEC's discounting from those list prices. Tr. 278. BEC refused to cooperate. Tr. 86.

Hartwell then enlisted Sharp's aid as price policeman, complaining to Sharp that he had lost the Tenneco account because of BEC's "price cutting". PX 39, Tr. 88-90. Sharp's representative thereafter instructed BEC "to maintain the correct discount range" on the Tenneco account. Tr. 91.

Hartwell told Sharp that it was "intolerable to compete with a heavy discounter," Tr. 287, and Sharp agreed to

cancel BEC to solve this problem, Tr. 287-90, 586, 587, 1355-56. Sharp says that Hartwell merely presented Sharp with a choice between Hartwell and BEC. But Hartwell expressly asked that BEC be terminated because BEC was continuing its price cutting. Hartwell did not merely complain about not having an exclusive distributorship in Houston. He wanted to eliminate discounting—the "very essence of competition" in a free market. *See Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 106 S. Ct. 1348, 1351 (1986).

Significantly, the record is devoid of any evidence that Sharp complained to BEC about lack of pre-sale promotional activity, such as advertising or customer sales visits. Nor did Hartwell's complaints to Sharp concern such matters. *See, e.g.*, Tr. 934 (Hartwell's primary complaint concerned BEC's "price cutting"). Rather, Sharp and Hartwell targeted BEC's unwillingness to avoid price competition.[4]

D. Effect on Competition.

Sharp implies that its brand was struggling for recognition. In fact, Sharp was the "worldwide and United States" "leader" in the calculator industry. PX 10. Contrary to Sharp's assertion that interbrand competition was "fierce", the evidence shows that Sharp had promised its competitors not to enter "into a meaningless price-cutting war" in order to "set an example for the industry." *Id.*

Equally groundless is Sharp's contention that price competition remained vigorous after BEC's termination.

4. Sharp had attempted to coerce BEC to avoid discounting even before Hartwell became a dealer—when BEC was the only dealer in Houston and hardly in a position to "free ride" on any other dealer's sales efforts. *See* Tr. 73-77, 239-40, PX 52, Tr. 244 (Sharp complained that BEC was "messing up" the market), Tr. 81 (Sharp threatened to cancel BEC unless he "clean[ed] up [his] pricing structure").

The price decline cited by Sharp says little about the vigor of price competition. Prices would have been even lower had BEC remained in the market. More telling is the substantial increase in Hartwell's gross margins following BEC's termination. PX 119; Tr. 389-91, 1156. Hartwell's avowed policy was to sell at Sharp's suggested list prices, and he adhered to that policy in the eleven years following BEC's termination. Tr. 294-95, 296, 398.

II. This Court Has Not Confined Resale Price Maintenance To Agreements to Set Prices "At Some Level."

This Court has never held that direct agreement on resale prices is the only form that *per se* unlawful resale price maintenance may take. To the contrary, the Sherman Act is also violated when a supplier conspires with its dealers to prevent a competing dealer from undercutting suggested resale prices. Sharp nevertheless contends that no per se violation occurred here since Hartwell remained "free" to engage in price competition. The fallacy of such analysis is obvious. By focusing only upon *Hartwell's* theoretical "freedom" to discount, Sharp ignores the purpose and effect of the conspiracy—to destroy *BEC's* freedom to discount. As a direct result of the conspiracy, BEC could no longer exercise *its* right to price independently.

To support its very narrow view of price fixing, Sharp resorts to smoke-and-mirror use of authorities.[5] Sharp

5. For instance, Sharp quotes from the Government's brief opposing BEC's petition:

> This Court has applied the per se rule against resale price maintenance *only* to situations in which the evidence showed that the manufacturer or wholesaler "dictat[ed] the prices charged by" a wholesaler or retailer. *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. [97,] 103 [(1980)]. . . .

Sharp Br. at 16 (quoting from U.S. Br. at 8) (emphasis added). Actually, *Midcal* does not say that the per se rule applies "only"

also distorts the holding in *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960), which cannot be harmonized with the decision below. At most, Sharp acknowledges that the *Parke, Davis* test requires no "direct evidence of an agreement on prices. . . ." Sharp Br. at 18. But *Parke, Davis* plainly rejected any requirement of actual agreement on prices. Writing for the majority, Justice Brennan carefully reviewed the per se rule's evolution regarding resale price maintenance. He observed the substantial limiting of *United States v. Colgate & Co.*, 250 U.S. 300 (1919), in which the Court had found no resale price maintenance absent an actual agreement obligating dealers to resell at fixed prices. Summing up, Justice Brennan wrote:

> [A]n unlawful combination is not just such as arises from a price maintenance agreement, express or implied; such a combination is also organized if the producer secures adherence to his suggested prices by means which go beyond his mere declination to sell to a customer who will not observe his announced policy.

362 U.S. at 43. Parke, Davis violated this test by "involving . . . wholesalers to stop the flow of . . . products to . . . retailers, thereby inducing retailers' adherence to its suggested retail prices. . . ." *Id.* at 45.[6]

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when a supplier actually requires dealers to charge prices by direct agreement. Rather, in discussing California's system for wine pricing, this Court merely observed that "[t]he wine producer holds the power to prevent price competition by dictating the prices charged by wholesalers." 445 U.S. at 103. In other words, the Government (and Sharp) plucked language out of context and attributed to it a meaning not expressed or even implied by the Court.

6. Attempting to buttress its interpretation of *Parke, Davis*, Sharp deftly quotes from *Ventsch v. Texaco, Inc.*, 630 F.2d 46 (2d Cir. 1980). Sharp Br. at 18. The actual language of the case reveals that the court merely recited *examples* of means by which resale price maintenance could be proven, not the exclusive means for proving it.

According to Sharp, *Parke, Davis* requires proof "that remaining dealers charged a price directed by the supplier. . . ." Sharp Br. at 18. But *Parke, Davis* cannot mean that remaining dealers must actually agree to charge fixed prices, or else the Court's explicit rejection of this element would be nonsensical. Rather, a plaintiff need only prove that his supplier and others conspired to enforce suggested resale prices—for example, by agreeing to terminate a dealer who refuses to comply, precisely the conduct found by the jury here. Like the defendants in *Parke, Davis*, Sharp and Hartwell conspired to stop the flow of Sharp calculators to BEC in order to end its non-compliance with Sharp's suggested retail prices. Given proof of an agreement that stopped *BEC's* price cutting, it would be pointless to require BEC to prove further that *Hartwell's* prices were directed by Sharp.

Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984), also cannot be read to require an agreement on price "at some level," despite Sharp's stringing together quotes taken out of context. The Court neither stated nor suggested that vertical price fixing must take the form of direct agreement on prices.[7] Significantly, *Monsanto* does not overrule or attempt to distinguish *Parke, Davis*. The Court addressed the evidentiary standard for proving

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7. Sharp cannot reasonably rely on dictum in footnote 9 of *Monsanto*, which says that resale price maintenance cannot be inferred from mere evidence that a distributor acquiesced in suggested resale prices. Read in context, the footnote merely relates to the "acquiescence" theory of resale price maintenance. *See, e.g.*, Albrecht v. Herald Co., 390 U.S. 145, 151 n.6 (1963); Arnott v. American Oil Co., 609 F.2d 873 (8th Cir. 1979), *cert. denied*, 446 U.S. 918 (1980). Plainly, the footnote does not set forth the exclusive means by which vertical price fixing may be proven.

vertical collusion, not the precise form an agreement must take in order to constitute resale price maintenance.[8]

Finally, Sharp relies on several post-*Monsanto* cases supposedly rejecting a theory of resale price maintenance predicated upon "an agreement between a supplier and a dealer that is 'price-related,' or 'price-motivated'. . . ." But some of these cases actually say just the opposite. For example, in the lead case cited by Sharp—*McCabe's Furniture, Inc. v. La-Z-Boy Chair Co.*, 798 F.2d 323, 329 (8th Cir.), *petition for cert. filed*, 55 U.S.L.W. 3495 (Dec. 29, 1986) (No. 86-1101), the Court said: "The distinction emphasized in *Monsanto* between per se and rule of reason illegality . . . must turn ultimately on motive: on whether the manufacturer and nonterminated dealer conspired to terminate the plaintiff *intending* to affect price competition, or nonprice competition." *Id.* at 329 (emphasis in original). Likewise, in *Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc.*, 824 F.2d 582 (8th Cir. 1987), also cited by Sharp, the court read *Monsanto* to require proof of a "price-related" conspiracy. *Id.* at 589 (emphasis added). The jury finding in the instant case meets this standard precisely.

III. Against Explicit Congressional Intent, the Decision Below Would Trivialize and Dilute the Per Se Rule Against Vertical Price Fixing.

The decision below creates a substantial loophole in the prohibition against vertical price fixing. If dealers are permitted to enter into agreements with suppliers to eliminate competitors who refuse to fix prices, the per se rule would

8. The lower court decisions cited at Sharp Br. 16 n.10, some of which concern nonprice restraints, do not address the issue presented here.

be reduced to a triviality. Although agreements to charge prices "at some level" would still be nominally per se illegal, the same result could easily be accomplished by agreeing to eliminate discounters.

Congress has unmistakably opposed any such trivialization of the *per se* rule.[9] BEC Br. at 36-42. Only three years ago Congress explicitly rejected a restrictive interpretation of the *per se* rule that would have required an actual agreement to set prices. *See* Departments of Commerce, Justice and State, the Judiciary and Related Agencies Appropriation Act, 1986, Pub. L. No. 99-180, 99 Stat. 1136, 1169-70 (1985). This is precisely the requirement imposed by the decision below.

Sharp's silence in response to the resounding evidence of Congressional intent is deafening. Sharp merely replies that since the *per se* rule against vertical price fixing was initially created by the Court, the Court should be able to change the rule. Construction of the antitrust laws, however, requires deference to legislative intent and recognition of long-standing congressional ratification of the *per se* rule. *See Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 51 n.18 (1977); *Jefferson County Pharmaceutical Ass'n v. Abbott Laboratories*, 460 U.S. 150, 170 (1983); *Square D Co. v. Niagara Frontier Tariff Bureau*, 106 S. Ct. 1922, 1927-28 (1986).[10]

9. In 1983 Congress enacted legislation amending the Department's appropriations in order to prevent it from engaging in any activity "the purpose of which is to overturn or alter the *per se* prohibition of resale price maintenance under the Federal Antitrust Laws." Pub. L. No. 98-166, § 510, 97 Stat. 1071, 1102 (1983). The most recent appropriations legislation for the Department of Justice contains a similar restriction. Departments of Commerce, Justice and State, the Judiciary and Related Agencies Appropriation Act, 1987, § 605, enacted into law as part of the Continuing Appropriations, 1987, Pub. L. No. 99-591 (1987).

10. Sharp's reliance on *Sylvania*, Sharp Br. at 45, is disingenuous. *Sylvania* explicitly noted that "Congress recently has expressed its

Curiously, Sharp alludes to pending legislation that would, among other things, codify the *per se* rule against vertical price fixing. The Senate bill—the Retail Competition Enforcement Act of 1987, S. 430, 100th Cong., 1st Sess., 133 Cong. Rec. 1484 (1987)—was favorably voted out of the Senate Judiciary Committee in August 1987, and awaits the Committee's report before proceeding to the full Senate. The similar House bill—the Freedom from Vertical Price Fixing Act of 1987—H.R. 585, 100th Cong., 1st Sess. (1987)—was passed by the House of Representatives by voice vote on November 9, 1987.

Although pending legislation may be a less sure guide to congressional intent than legislation actually enacted, the House Report accompanying H.R. 585, H.R. Rep. No. 100-421, 100th Cong., 1st Sess. (1987), again demonstrates Congress' intent to retain an unqualified ban on vertical price fixing.[11] The Report criticizes cases, including the decision below, holding that an agreement to protect a competitor from discount competition is not subject to the *per se* rule against vertical price fixing. *Id.* at 23. The Report makes clear that this is not now and never has been the view of Congress. The bill "restates plainly and unequivocally that *all forms* of resale price maintenance are illegal *per se* under the antitrust laws." *Id.* at 38, 33. Thus, a violation of the *per se* rule

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approval of a *per se* analysis of vertical price restrictions by repealing those provisions of the Miller-Tydings and McGuire Acts allowing [vertical price fixing]. . . ." 433 U.S. at 51 n.18. The portion of *Sylvania* relied upon by Sharp, 433 U.S. at n.27, addresses only the issue whether a court or jury can appropriately balance intra- and interbrand competition effects of nonprice restraints.

11. Copies of this Report have been lodged with the clerk for the Court's convenience. The Report observes that the prohibition against vertical price fixing is an important feature of "national competition policy where Congress has historically demonstrated an unequivocal intent to assert its role as the 'ultimate antitrust policy maker'." H.R. Rep. No. 100-421 at 4.

will lie, *inter alia*, "where a conspiracy exists between a supplier and distributor to terminate or cut off supply to a second distributor because of the second distributor's pricing policies." *Id.* at 38.

IV. Rule of Reason Treatment of Nonprice Restraints Does Not Prevent Per Se Treatment of a Conspiracy Aimed Directly at Elimination of Price Competition.

A. Sharp Fails to Recognize the Critical Distinction Between Price and Nonprice Restraints.

Sharp argues at length about the putative pro-competitive benefits of vertical restrictions, including the conduct at issue here. The short answer to these arguments is that this Court swept them away as to vertical price restraints in *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 51 n.18 (1977). In discussing the "market impact of vertical restrictions," the Court made clear that it was concerned

> only with non-price vertical restrictions. The *per se* illegality of price restrictions has been established firmly for many years and involves significantly different questions of analysis and policy. As Mr. Justice White notes . . . some commentators have argued that the manufacturer's motivation for imposing vertical price restrictions may be the same as for nonprice restrictions. There are, however, significant differences that could easily justify different treatment.

Id.; accord Filco v. Amana Refrigeration, Inc., 709 F.2d 1257, 1265 n.2 (9th Cir.), *cert. denied*, 464 U.S. 956 (1983).

Congress and others have recognized that resale price maintenance "leads to higher prices and lower output

just as horizontal price-fixing does." *See e.g.*, Shores, *Vertical Price-Fixing and the Contract Conundrum: Beyond Monsanto*, 54 Fordham L. Rev. 377, 412 (1985-86); Jacobson, *On Terminating Price-Cutting Distributors in Response to Competitors' Complaints*, 49 Brooklyn L. Rev. 677, 684 (1982-83) (cites Congressional and other authority); H.R. Rep. No. 341, 94th Cong., 1st Sess. 3 (1975) ("beyond dispute that resale price maintenance increases the cost of products to consumers"). For this reason, in the context of naked restraints on price competition, the horizontal/vertical distinction has little significance. Both horizontal and vertical price restraints are subject to the *per se* rule, and they are treated differently only with respect to the *Monsanto* requirement of unambiguous evidence proving vertical collusion. Accordingly, cases broadly defining price-fixing in the horizontal context are persuasive in the area of vertical price restraints as well.

Whatever else may be said about an agreement to eliminate price cutting, it is plainly a restraint aimed directly at price competition. Sharp seeks to avoid this obvious fact by criticizing the use of intent as a means for categorizing conduct. Such criticism defies decades of well-accepted antitrust doctrine. The courts have long recognized intent as an important basis for delineating conduct subject to antitrust challenge. For example, specific *intent* to destroy competition or build monoply" is a critical element of attempting to monopolize in violation of Section 2 of the Sherman Act. *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594, 626 (1953) (emphasis added). Proof of conspiracy entails establishing "conscious commitment to a common scheme *designed* to achieve an unlawful objective." *Monsanto, supra* at 764 (emphasis added). In the horizontal price-fixing area, courts focus on *purpose*, because it tends

to show effect, in separating price from nonprice restraints. *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1, 19-20 (1979).

Vertical price restraints are no different. Finders of fact are capable of distinguishing between dealer terminations for performance reasons—such as failure to advertise—and dealer terminations pursuant to an agreement to eliminate price competition. Such fact-finding is no more difficult than discerning intent in any other antitrust context or, for that matter, in the numerous other areas of law, including criminal law, where proof of intent is required.

B. Conclusory, Speculative Assertions About Pro-Competitive Effects Cannot Justify Evisceration of the Per Se Rule Against Vertical Price Fixing.

If the decision below is affirmed, all but the most blatant forms of vertical price fixing will escape *per se* treatment. To justify this abdication of the *per se* rule, Sharp resorts to conclusory, speculative assertions as to pro-competitive motives of suppliers and supposed benefits of eliminating free riding. Not only do precedent and Congressional intent contradict such contentions, but Sharp's arguments also have insufficient basis in fact to warrant what would amount to a substantial repeal of the *per se* rule.

According to Sharp, suppliers have no real interest in maintaining resale prices, since a vertical agreement benefits a supplier only if it increases sales of the suppliers' product. This conclusory assertion ignores reasons that a supplier would serve as price policemen for dealers who wish to avoid price competition. First, as noted in *Sylvania*, industry-wide resale price maintenance may facilitate car-

telizing. 433 U.S. at 51 n.18. Indeed, the evidence in this case suggests just such a motive. *See* PX 10. Second, over the long run, aggressive price competition at the retail level will drive down prices at the wholesale level as well. "The manufacturer cannot continue over time to charge a relatively high wholesale price regardless of the effects of dealer competition on the level of retail prices." Pitofsky, *In Defense of Discounters: The No-Frills Case for a Per Se Rule Against Vertical Price Fixing*, 71 Geo. L. J. 1487, 1492 (1983); *see Albrecht v. Herald Co.*, 390 U.S. 145, 151 n.7 (1968).

But Sharp's main thrust aims at the alleged benefits of eliminating "free riders" from the market. Turning fundamental Sherman Act concerns upside down, Sharp asserts that price cutting is anticompetitive, since it purportedly undercuts dealers who offer "full service" and that "service" competition is more important than price competition. Such "free rider" arguments, at least in the area of price restraints, mask a disdain for "the very essence of competition." *Cf. Matsushita*, 106 S. Ct. at 1351. Price competition can always be labelled as free riding. Any dealer who is more efficient—who can sell effectively with less overhead expense—can be branded a "free rider." Thus, removing *per se* treatment from naked price restraints on the basis of "free rider" concerns would turn Sherman Act policy on its head. Pitofsky, *supra* at 1492-93 ("To deny [so-called free riders] access to products because they are aggressive in pricing (and perhaps more efficient as well) hardly seems to be a service to consumers, or a vote of confidence in the competitive process.").

The free rider rationale also suffers from a lack of significant empirical basis. As noted by one commentator:

> . . . [D]espite the emphasis free riding has received in the economic literature and in recent decisions, its actual role in vertical price fixing is speculative. Indeed, Telser, who first developed the free rider theory, acknowledged that while it provides a rational explanation for resale price maintenance, its actual significance has not been established through empirical evidence and is unknown.

Shores, *supra* at 402. Thus, the "free rider" rationale, at least as it relates to price restraints, bears more the earmarks of ideology rather than of economic science.

Moreover, vertical price fixing is neither necessary nor sufficient to address the problems associated with the hypothetical "free rider" encountered in law review debates. Suppliers can deal with the free riding problem by means far less restrictive and more effective than outright agreements eliminating price cutting. The essence of "free riding" is a dealer's failure to provide services or advertising desired by the manufacturer. Rather than indirectly and overbroadly policing discounting through collusive dealer termination, a supplier can directly correct the problem by contractually requiring each dealer to provide a minimum level of advertising or service. Also, subject to the rule of reason, the manufacturer can impose various nonprice restraints, such as limiting the number of dealers in a given territory and restricting the sales territories and locations. Pitofsky, *supra* at 1493; H.R. Rep. No. 100-421 at 13 (" 'free rider' problem . . . can be addressed most effectively through . . . contractual commitments, without the harm to consumers that ensues from . . . vertical price fixing."). Furthermore, as noted by the House of Representatives, "absent a contractual commitment, resale price maintenance would, in any event, not eliminate free riders since full price retailers could still disregard dealer service and promotion standards." *Id.*

Finally, the "free rider" rationale, as applied to justify price restraints, assumes that customers really want or

need the services supposedly induced by the elimination of price cutting. Each retailer brings his goods to the market in a different way with a different emphasis. Some dealers emphasize price, and others emphasize service. Collusive termination of dealers who offer better prices but less service destroys consumers' freedom to set their own priorities. See Pitofsky, *supra* at 1492-93.

The instant case well illustrates the danger of extending the "free rider" rationale to justify collusive dealer terminations aimed at eliminating price cutting. The "free rider" concerns in this case are illusory. Sharp never complained to BEC regarding advertising or presale promotional activities. Here the "free rider" argument sprang to life in the bright light of hindsight rather than in any contemporaneous Sharp effort to induce dealer services. *Cf. Com-Tel, Inc. v. DuKane Corp.*, 669 F.2d 404, 410 (6th Cir. 1982) (*Sylvania* considerations inapplicable to boycott where suppliers' marketing strategy tolerated certain amount of intrabrand competition).

Asserting that interbrand competition may act as a "check" on higher prices does not give the "free rider" rationale any more credence as a justification for killing intrabrand price competition. As Justice Brennan noted in *White Motor Co. v. United States*, 372 U.S. 253, 268 (1963): "Resale price maintenance is not only designed to, but almost invariably does in fact, reduce price competition not only *among* sellers of the affected product, but quite as much *between* that product and competing brands." (quoted with approval in *Sylvania*, 433 U.S. at 51 n. 18). Indeed, if interbrand price competition were a check on the harmful effects of vertical price restraints, there would be no point to imposing the vertical price restraint in the first place, since interbrand competitors could also "free ride."

See W. Comanor, *Vertical Price-Fixing, Vertical Market Restrictions, and the New Antitrust Policy*, 98 Harv. L. Rev. 983, 1000 (1985).

V. The Court May Properly Consider Support for the Per Se Rule Found in the Group Boycott Line of Authority.

BEC cited group boycott cases such as *United States v. General Motors Corp.*, 384 U.S. 127 (1966) and *Victorian House, Inc. v. Fisher Camuto Corp.*, 769 F.2d 466 (8th Cir. 1985) to the Fifth Circuit and in its petition. *See* BEC Pet. at 9-11. In any event, citation of additional legal authorities for reversing the decision below does not raise additional questions in violation of Sup. Ct. R. 21.1. As Justice Harlan recognized in *General Motors*, there is no bright line distinction between vertical price fixing to eliminate discounts and group boycotts to eliminate discounters. 384 U.S. at 148-49 (Harlan, J. concurring).[12]

Sharp argues that the group boycott cases are inapplicable here because they involved some horizontal element. BEC does not dispute the presence of a horizontal element. BEC Br. at 32-35. But neither this Court's precedents nor logic require horizontal collusion for application of the *per se* rule. The key factor in each *General Motors*' type boycott case is the exercise of vertical leverage against the targeted dealer. *Id.*

---

12. Sharp makes the straw man argument that all dealer terminations "at the behest" of another dealer would involve a group boycott under *General Motors* and related boycott cases. But *General Motors* prohibits only *collaborative* action to eliminate a competitor. 384 U.S. at 145-46 (exclusion of traders from the market by means of "combination or conspiracy" constitutes *per se* violation). Here, BEC was terminated pursuant to an actual agreement between Sharp and Hartwell to eliminate BEC's discounting.

VI. The Validity of the Per Se Rule Is Not Properly Before the Court.

Sharp devotes a substantial portion of its brief to arguing that the *per se* rule against vertical price fixing should be overturned. But this Court has not granted Sharp's cross-petition for certiorari, No. 85-2094, which raises this issue. Thus Sharp's arguments in this regard are not properly before the Court.[13]

For the reasons expressed above, this Court should reverse the Fifth Circuit's decision below and reinstate the judgment of the district court.[14]

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13. Moreover, as outlined in BEC's brief in opposition to Sharp's cross petition, there are compelling reasons for not granting certiorari on this issue. Foremost among them is that Congress has repeatedly and unambiguously ratified the *per se* rule against vertical price fixing in the seventy-seven years since *Dr. Miles*. For other reasons to retain the *per se* rule against vertical price fixing, *see* BEC Br. in Opp. to Cross-Pet. at 15-17; L. Sullivan, Handbook of the Law of Antitrust (1977) 385-88; D. Marks and J. Jacobson, Price-fixing: An Overview, Antitrust Bulletin (Spring 1985) 199, 245-251; H.R. Rep. No. 100-421 at 11-13.

14. Contrary to Sharp's contention, error in the exclusion of two exhibits (DX 52 and 53) does not require a new trial. Such error was not "inconsistent with substantial justice," *see* Fed. R. Civ. P. 61, and constituted harmless error since the excluded exhibits were merely cumulative, *see* Fed. R. Civ. P. 403; Sharp Br. at 6 (referring to admitted evidence cumulative of DX 52 and 53). At the very least, because the Fifth Circuit did not determine whether exclusion of the exhibits was inconsistent with substantial justice or constituted harmless error, the Court should remand the case to the Fifth Circuit for consideration of this issue before ordering a new trial.

Respectfully submitted,

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No. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF OF AMICUS CURIAE K MART CORPORATION IN SUPPORT OF PETITIONER

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August 22, 1987

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QUESTION PRESENTED

Whether Section 1 of the Sherman Act allows a supplier to conspire and agree with a full-price retailer to terminate a discount retailer for the purpose of eliminating price competition.

PARTIES TO THE PROCEEDING BELOW

Plaintiff-Appellee: Business Electronics Corporation

Defendant-Appellant: Sharp Electronics Corporation

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IN THE

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OCTOBER TERM, 1987

No. 85-1910

BUSINESS ELECTRONICS CORPORATION,
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v.

SHARP ELECTRONICS CORPORATION

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF OF AMICUS CURIAE K MART CORPORATION IN SUPPORT OF PETITIONER

K mart Corporation ("K mart") respectfully submits this brief as amicus curiae in support of petitioner Business Electronics Corporation.[1]

INTEREST OF THE AMICUS CURIAE

K mart operates more than 2,000 discount department stores in the United States. It is K mart's goal to offer

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[1] Pursuant to Supreme Court Rule 36.2, the parties have consented to the filing of this brief. K mart has filed their written consents with the Clerk.

the consumer quality name-brand merchandise at prices lower than those established by manufacturers or followed by other retailers. Despite its size and purchasing power, K mart is often denied access to merchandise because of collusion between a manufacturer and its independent distributors or because a full-price retailer has solicited or coerced a manufacturer's agreement not to deal with K mart because K mart is a discounter.

Given the recent lack of antitrust enforcement by the Federal Trade Commission and Department of Justice, K mart has vindicated its commercial freedom by filing private antitrust actions.[2] However, even this remedy is now threatened by some courts which, like the Fifth Circuit below, have misconstrued the decision in *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), as condoning all manner of vertical price-fixing conspiracies.

STATEMENT OF THE CASE[3]

Sharp Electronics Corporation ("Sharp") is a supplier of electronic calculators distributed through a network of retail dealers. 780 F.2d at 1214. Business Electronics Corporation ("BEC") was the only authorized Sharp dealer in Houston for several years until Sharp appointed Hartwell's Office World ("Hartwell") as a Sharp dealer in the same area. 780 F.2d at 1214-1215. After complaining to Sharp for over a year about BEC's discounting practices, Hartwell presented an ultimatum to Sharp: if Sharp would not terminate BEC within 30 days, Hartwell would quit as a Sharp dealer. 780 F.2d at 1215. Sharp then terminated BEC, leaving Hartwell as the only Sharp dealer in Houston. 780 F.2d at 1215.

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[2] *See, e.g., K mart Corp. v. Rachel Perry, Inc.*, No. 83-CV-4784-DT (E.D. Mich.) (September 5, 1985 consent order prohibits Rachel Perry from conspiring with distributors to deprive K mart of access to Rachel Perry products).

[3] Facts are taken from and cited to the reported decision of the Fifth Circuit in this case, 780 F.2d 1212 (5th Cir. 1986).

The jury in this case was presented with a clear factual choice: was BEC terminated because it was a marginal retailer who failed to meet Sharp's sales quotas; or was BEC terminated when Hartwell, a full-price retailer, convinced Sharp to eliminate BEC, the only source of intrabrand retail price competition in Houston, because of its discounting. 780 F.2d at 1215. In response to very specific interrogatories and instructions, the jury concluded that BEC was terminated pursuant to "an agreement or understanding between Sharp and Hartwell to terminate [BEC] as a Sharp dealer because of [BEC's] price-cutting." 780 F.2d at 1215.

The Fifth Circuit held that this finding was insufficient. Absent proof of an agreement between Sharp and Hartwell "to set [Hartwell's] prices at some level," the court of appeals held that their vertical conspiracy to eliminate a competitor in order to end price competition was not *per se* illegal under Section 1 of the Sherman Act. 780 F.2d at 1218.

SUMMARY OF ARGUMENT

Section 1 of the Sherman Act forbids "every contract, combination . . . or conspiracy, in restraint of trade or commerce." 15 U.S.C. § 1. Historically, this provision has been read as forbidding absolutely price-fixing agreements, whether horizontal, that is between competitors at the same functional level of distribution, or vertical, that is between companies at different levels of distribution.[4]

Such absolute condemnation has been reserved for conduct most damaging to competition and economic freedom, and the conduct found by the jury in this case warrants absolute condemnation. Many less restrictive and perfectly legal alternatives were available for Sharp to

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[4] Vertical price fixing is often called "resale price maintenance" because it is generally an effort by a manufacturer to maintain or engineer resale prices at a level artificially higher than the prices which would otherwise prevail in a competitive market.

accomplish its legitimate goals in the Houston market, but Hartwell and Sharp chose improper means to accomplish an improper purpose. Their conspiracy was more damaging to competition than other conduct which is *per se* illegal. For example, Sharp could have legally terminated BEC if BEC had failed to meet sales quotas; the jury found, however, that Sharp's purpose was to eliminate retail price competition. Sharp could have legally demanded that BEC provide the services and promotion which Sharp expected of its dealers; the jury found, however, that Sharp terminated BEC because of its low prices, not its level of services. Sharp could have legally adopted a unilaterally determined suggested retail price and unilaterally terminated BEC for not adhering to it; the jury found, however, that Sharp acted at the insistence of and in collusion with Hartwell, BEC's competitor.[5]

In short, Hartwell succeeded in eliminating BEC, its only competitor, not by competing fairly or offering the consumer a superior combination of price and service, but by conspiring with and threatening Sharp.[6]

Compare this resale price maintenance conspiracy which the jury condemned and the Fifth Circuit condoned

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[5] The termination was also preceded by various threats and coercion which are not protected by *United States v. Colgate & Co.*, 250 U.S. 300 (1919). *See United States v. Parke, Davis & Co.*, 362 U.S. 29, 46 (1960), and *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 765 (1984).

[6] There appears to have been no claim that Sharp dealers provided warranty service or other functions which could justify non-price vertical restraints. *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977). The jury apparently rejected Hartwell's contention that BEC was taking unfair advantage of Hartwell's "products promotion." *See* 780 F.2d at 1215. Likewise, there appears to have been no contention that the market for electronic calculators was such to justify elaborate vertical restraints. *See United States v. Jerrold Electronics Corp.*, 187 F. Supp. 545 (E.D. Pa. 1960), *aff'd per curiam*, 365 U.S. 567 (1961).

with other possible schemes of eliminating price competition which would be absolutely forbidden by Section 1 of the Sherman Act but far less pernicious than the activity approved by the Fifth Circuit: (1) BEC could have expressly agreed with Sharp to charge Sharp's suggested list price; illegal *per se*; or (2) BEC could have agreed with Hartwell to charge Sharp's suggested list price; also illegal *per se*.

In either of these scenarios, the possibility would have remained for BEC and Hartwell to cheat or renege on their price-fixing agreements; two retail competitors would have remained in the Houston market and competed at least in non-price areas. Instead, the Fifth Circuit has endowed Hartwell with a monopolistic freedom to overcharge the consumer.

Two parties, acting collusively, made an agreement to eliminate price competition and have successfully carried it out under the Fifth Circuit ruling. Such a result is not consistent with either this Court's construction of the antitrust laws or Congressional expressions of its intent. Moreover, it is inimical to the economic well-being of the American public.

ARGUMENT

I. The Antitrust Laws Have Always Been Construed As Preserving Commercial Independence At All Levels Of Distribution

The Fifth Circuit has drawn an ephemeral distinction between agreements to fix a particular price and agreements to destroy price competition. According to the Fifth Circuit, it is unlawful for a manufacturer and its dealer to conspire to set a particular price in the marketplace, but it is completely lawful for them to agree to end all price competition in the marketplace. This decision undercuts better than 75 years of the administration of the Sherman Act.

Since at least 1911, resale price maintenance has been illegal *per se* under Section 1 of the Sherman Act. *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911).[7] The holding in *Dr. Miles* that an agreement between a manufacturer and its dealers to maintain a minimum retail price violated the Sherman Act came despite vigorous arguments that discounters were "knaves" and that a manufacturer knew best what price the consumer would or should pay. 220 U.S. at 412 (Holmes, J., dissenting). The Court concluded that Dr. Miles, "having sold its product at prices satisfactory to itself, the public is entitled to whatever advantage may be derived from competition in the subsequent traffic." 220 U.S. at 409. The Fifth Circuit apparently disagrees.

Judicial condemnation of vertical price fixing was a logical extension of the earliest Sherman Act decisions which recognized that agreements which gave the conspirators "the power to charge unreasonable prices" were absolutely illegal both at common law and under the Sherman Act. *United States v. Addyston Pipe & Steel Co.*, 85 Fed. 271, 293 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

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[7] *See United States v. Colgate & Co.*, 250 U.S. 300 (1919); *United States v. A. Schrader's Son, Inc.*, 252 U.S. 85 (1920); *FTC v. Beech-Nut Packing Co.*, 257 U.S. 441 (1922); *United States v. Line Material Co.*, 333 U.S. 287 (1948); *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211 (1951); *United States v. Parke-Davis & Co.*, 362 U.S. 29 (1960); *Simpson v. Union Oil Co.*, 377 U.S. 13 (1964); *California Retail Liquor Dealers v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980); *Rice v. Norman Williams Co.*, 458 U.S. 654 (1982); *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984); *324 Liquor Corp. v. Duffy*, 107 S.Ct. 720 (1987). In the past decade, the Court has distinguished between vertical agreements to set prices, which are *per se* illegal, *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 761 (1984); *324 Liquor Corp. v. Duffy*, 107 S.Ct. 720, 724 (1987), and vertical agreements on non-price restrictions, which are judged under the rule of reason. *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

In the cases that followed *Dr. Miles*, several threads emerged: First, a seller's freedom to choose a resale price was recognized as a most critical element of competition.[8] Second, it was *per se* illegal for a manufacturer (outside the narrow price "suggestion" boundaries of *Colgate*) to fix a particular price, set a minimum price, establish a maximum price or otherwise restrict the pricing discretion of its distributors or dealers.[9] Third, collusion to fix prices or eliminate price competition was *per se* illegal.[10]

Justice Stevens has explained why price competition receives such extraordinary protection:

> Price is the 'central nervous system of the economy,' and an agreement that 'interfere[s] with the setting of price by free market forces' is illegal on its face.

National Society of Professional Engineers v. United States, 435 U.S. 679, 692 (1978) (citations omitted).[11] This reasoning applies at the retail level, not just to manufacturers:

> It is in the sound commercial interests of the retail purchasers of goods and services to obtain the lowest price possible within the framework of our competitive private enterprise system. The essence of the

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[8] *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211, 213 (1950); *Simpson v. Union Oil Co.*, 377 U.S. 13, 16 (1964); *Albrecht v. Herald Co.*, 390 U.S. 145, 152 (1968).

[9] *Albrecht v. Herald Co.*, 390 U.S. 145, 152 (1968) (maximum prices); *United States v. Socony Vacuum Oil Co.*, 310 U.S. 150, 222 (1940) (range of prices).

[10] *Albrecht v. Herald Co.*, 390 U.S. 146 (1968); *United States v. General Motors Corp.*, 384 U.S. 127 (1967); *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960); *Klor's, Inc. v. Broadway Hale Stores, Inc.*, 359 U.S. 207 (1959).

[11] As the Court has also recognized, since retail price maintenance is absolutely forbidden, it is not saved by the euphemistic labels which the conspirators may adopt. *E.g., Simpson v. Union Oil Co.*, 377 U.S. 13 (1964) (sham consignment system).

antitrust laws is to ensure fair price competition in an open market.

Reiter v. Sonotone Corp., 442 U.S. 330, 342 (1979).

In these and many other decisions, the Court carefully considered and rejected the same economic justifications which were rejected in *Dr. Miles* and which are proffered to justify vertical price fixing today.[12]

Since resale price maintenance continues to be *per se* illegal, what constitutes resale price maintenance? In this case, Sharp and Hartwell agreed to terminate BEC in order to eliminate price competition. As a result, Hartwell, who at least "usually" charged full list prices, became the only authorized Sharp dealer in Houston. 780 F.2d at 1215. Consumers were left with no choice because Hartwell had no competition in price or services. But the Fifth Circuit held that this would not be *per se* illegal unless BEC could prove that Hartwell and Sharp expressly or impliedly "agree[d] to set [Hartwell's] price at some level, though not a specific one." 780 F.2d at 1218.

This has never been the law, either in horizontal or vertical price fixing conspiracy cases, and it would place an impossible burden on an antitrust plaintiff.

Price fixing is a federal felony crime under the Sherman Act. No manufacturer wishing to eliminate competition in pricing can be expected to draw up a written agreement or to list price levels as required by the Fifth Circuit. If the Fifth Circuit is affirmed, a large part of the protection which the Sherman Act has historically accorded to the public will be wiped out.

An agreement to eliminate discounters has the purpose and effect of setting resale prices even more effectively than an agreement on specific prices. Once discounters

[12] *See Simpson v. Union Oil Co.*, 377 U.S. 13, 19 n.6 (1964); *Albrecht v. Herald Co.*, 390 U.S. 145, 151 n.7 (1971).

have been eliminated, the colluding manufacturer and dealers can victimize the public at their leisure.

The Sherman Act has been characterized as a charter of economic freedom. Any vestige of marketplace freedom is effectively undermined when courts allow admitted conspirators to drive out of the market those who do not share their view of what the resale price should be.

A. Courts Have Always Condemned Vertical Conspiracies To Eliminate Price Competition As *Per Se* Illegal

In *United States v. General Motors Corp.*, 384 U.S. 127, 142-143 (1966), Justice Fortas spoke for a unanimous Court:

> [I]t has long been settled that explicit agreement is not a necessary part of a Sherman Act conspiracy . . . .

In his concurrence, Justice Harlan was more particular:

> [A] manufacturer cannot maintain resale prices by refusing to sell to those who do not follow his suggested price if the refusal is attended by concerted action with his customers . . . .

384 U.S. at 148. These statements of the law apply to the existence of the conspiracy as well as to its purpose; a conspiracy to fix prices requires neither an explicit agreement nor an agreement on a certain price.

1. *It Is* Per Se *Illegal To Conspire On Prices, Even If A Specific Price Is Not Set*

In several cases, the Court has ruled that it is not necessary for conspirators to set a specific price in order to violate Section 1 of the Sherman Act. For instance, in *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707, 719 (1944), the illegal agreement was simply that dealers would "sell at locally prevailing prices and only to the public." In *United States v. General Motors*

Corp., 384 U.S. 127, 147 (1966), the Court held that "the *per se* rule applies even when the effect upon prices is indirect."

This is true in both horizontal and vertical conspiracies. *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 222 (1940) ("[P]rices are fixed . . . if the range within which purchases or sales will be made is agreed upon, if the prices paid or charged are to be at a certain level or on ascending or descending scales, if they are to be uniform, or if by various formulae they are related to the market prices."); *United States v. Container Corp.*, 393 U.S. 333 (1969) (*per se* illegal to exchange price information for the purpose of stabilizing prices); *National Society of Professional Engineers v. United States*, 435 U.S. 679, 692 (1978) (*per se* illegal to agree not to negotiate on a price until after an engineer had been selected); *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 645, 647-648 (1980) (*per se* illegal to agree to eliminate credit terms or to use a specific method of quoting prices).

As recently as *Monsanto* in 1984, the Court held that warning discounters that they would not receive adequate shipments and notifying them that steps were being taken to get the market "in order" constituted "sufficient evidence for the jury reasonably to have concluded that Monsanto and some of its distributors were parties to an 'agreement' or 'conspiracy' to maintain resale prices and terminate price cutters." 465 U.S. at 765.

2. *It Is* Per Se *Illegal To Conspire To Eliminate A Discounter*

The motive which the jury found in this case has been a hallmark of conduct deemed *per se* illegal by this Court in the context of both horizontal and vertical conspiracies: "Elimination, by joint collaborative action, of discounters from access to the market is a *per se* violation of the [Sherman] Act." *United States v. General Motors Corp.*, 384 U.S. 127, 145 (1966).[13]

The illegal refusal to deal in *Klor's, Inc. v. Broadway Hale Stores, Inc.*, 359 U.S. 207, 213 (1959), was initiated by a Klor's competitor and was condemned because it deprived Klor's of merchandise, deprived suppliers of the opportunity to deal with Klor's and drove small retailers like Klor's out of business. 359 U.S. at 213.

These landmark cases are sometimes characterized as horizontal because either more than one retailer (in *General Motors*) or more than one supplier (in *Klor's*) participated in the conspiracy. The common horizontal element, however, is the participation of the victim's competitor in a conspiracy designed to eliminate price competition.[14] Thus, in condemning conspiracies between a supplier and a full-price dealer to terminate a discounter, courts of appeals have held that such conspiracies have a primarily horizontal purpose and effect which has always been viewed as *per se* illegal. *Victorian House, Inc. v. Fisher Camuto Corp.*, 769 F.2d 466, 469 (8th Cir. 1985); *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 168

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[13] The consent order in the treble damage action instituted by K mart against Rachel Perry expressly recited:

> [Rachel Perry] agrees that a joint collaborative effort precluding a price discounter from obtaining [Rachel Perry] products from distributors in order to fix, set, or influence resale prices constitutes a conspiracy in *per se* violation of Section 1 of the Sherman Act (15 U.S.C. § 1).

K mart Corp. v. Rachel Perry, Inc., No. 83-CV-4784-DT (E.D. Mich.) September 5, 1985 consent order ¶ 9.

[14] Even though a discounter, such as BEC, faces only one competitor, such as Hartwell, it should be no less illegal for that one competitor to conspire with a common supplier to eliminate the discounter. The effect of such a conspiracy is very pernicious because *all* price competition is eliminated at a single stroke: "it matters not that the complainant may be only one merchant." *Simpson v. Union Oil Co.*, 377 U.S. 13, 16 (1964), *citing Klor's*. *See Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979), where the court found *per se* illegality based on the request of a single dealer to terminate his price-cutting competitor.

(3d Cir. 1979); *Zidell Explorations, Inc. v. Conval Int'l, Ltd.*, 719 F.2d 1465, 1470 (9th Cir. 1983); *Com-Tel v. Dukane Corp.*, 669 F.2d 404, 411 (6th Cir. 1982).

As the Third Circuit said in *Cernuto*:

> By prevailing upon United and Lappin to terminate their contract with Cernuto, Famous effectively eliminated the threatened competition and was able to maintain prices at its own preferred levels. It is just this type of conduct that the antitrust laws were designed to reach.

595 F.2d 164, 169 (3d Cir. 1979). The Fifth Circuit ruling in the instant case sanctifies the fixing of resale prices by collusion between a manufacturer and a dealer just as surely as if these parties had agreed upon a specific price.

B. Courts Have Never Imposed Impossible Evidentiary Burdens On The Victims Of A Conspiracy

It is certainly implicit in the price-related complaints of a dealer that if a discounting competitor is terminated, the complaining dealer will charge a higher price. This is particularly true where the complaining dealer enjoys a position of sufficient strength vis-a-vis the manufacturer credibly to threaten resignation if the discounter is not terminated—as Hartwell did in this case.

A conspiratorial agreement need not be express or formal to violate the antitrust laws; it may be tacit or evidenced only by a course of conduct. *United States v. American Radiator & Standard Sanitary Corp.*, 433 F.2d 174 (3d Cir. 1970), *cert. denied*, 401 U.S. 948 (1971); *United States v. Consolidated Packaging Corp.*, 575 F.2d 117, 126 (7th Cir. 1978). As the Ninth Circuit has observed, "a knowing wink can mean more than words" in the context of a price fixing conspiracy; therefore, "it is not necessary to find an express agreement, either oral or written, in order to find a conspiracy . . . ." *Esco Corp.*

v. United States, 340 F.2d 1000, 1007, 1008 (9th Cir. 1965).

Since secrecy and concealment are the hallmarks of a conspiracy, an antitrust plaintiff has never been expected to prove its existence with the degree of certainty inherent in a breach of contract case.[15] Although, as the Court observed in *Monsanto*, a conspiracy finding cannot be based on "highly ambiguous evidence," 456 U.S. at 763, testimonial and documentary evidence of a "meeting of the minds in an unlawful arrangement" was a sufficient basis for the *Monsanto* jury's finding of an unlawful conspiracy. 465 U.S. at 764.

Moreover, the Court made it clear in *Monsanto* that the mere fact that evidence is subject to several interpretations does not warrant the entry of a directed verdict. As the Court said, "the choice between two reasonable interpretations of the testimony properly was left to the jury." 465 U.S. at 766 n.12. In the instant case, the Fifth Circuit would not allow the jury the proper latitude specified in *Monsanto*.

C. The Rule Of Law In *Dr. Miles* Will Not Stifle Legitimate Commercial Activity

Since 1975, when the Fair Trade laws were repealed, manufacturers and dealers have successfully conducted their affairs knowing that resale price maintenance was *per se* illegal. And there was no dearth of commercial activity in the Third, Fourth, Eighth and Ninth Circuits, which followed the strict *Cernuto* rule of law:

> [I]f a manufacturer deliberately withdraws its product from a price-cutting distributor at the re-

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[15] Similarly, antitrust plaintiffs face a lower burden of proof on the issue of damages, in recognition of the fact that the defendant is in control of and can effectively conceal the facts required for more rigorous proof. *J. Truett Payne Co. v. Chrysler Motors Corp.*, 451 U.S. 557, 566 (1981); *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 123 (1969).

> quest of a competing distributor as part of a conspiracy to protect the requesting distributor from price competition, the manufacturer has committed a per se violation of the antitrust laws.

Zidell Exploration, Inc. v. Conval Int'l, Ltd., 719 F.2d 1465, 1469 (9th Cir. 1983), *citing Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 170 (3d Cir. 1979).

In fact, the *per se* rule against conspiracies to eliminate price competition "provide[s] guidance to the business community and . . . minimize[s] the burdens on litigants and on the judicial system of the more complex rule-of-reason trials." *Continental T.V. Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 50 n.16 (1977). As the Court has also recognized, "without the *per se* rules, businessmen would be left with little to aid them in predicting [the outcome] in any particular case. . . ." *United States v. Topco Associates, Inc.*, 405 U.S. 596, 609 n.10 (1972).

The Court has increasingly recognized that price as well as non-price communications and complaints naturally travel from dealers to suppliers in the normal course of business, and that such communications should not be the sole basis for inferring an illegal conspiracy. *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 763-764 (1984).

The "plus factors" which the Court enumerated as sufficient in *Monsanto* were present in this case. Hartwell went beyond communication when it "presented an ultimatum to Sharp," 780 F.2d at 1215, threatening to resign if Sharp did not terminate BEC. The Court has always distinguished between acceptable communication and such improper coercion.[16]

On the other hand, the Fifth Circuit approach would make resale price maintenance, accomplished through dealer vendettas against discounters, presumptively legal.

[16] *Compare United States v. Colgate & Co.*, 250 U.S. 300 (1919), *with United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960).

It would be difficult, if not impossible, for a terminated dealer to prove by the preponderance of the evidence, that the conspiring dealer had agreed with the manufacturer to charge a particular price.

II. In The View Of Congress, The Antitrust Laws Absolutely Prohibit Vertical Conspiracies To Eliminate Price Competition Even When These Conspiracies Do Not Involve The Setting Of A Specific Price

When the Sherman Act was first debated, Congress recognized the evils of both resale price maintenance and conspiracies against discounters:

> [T]hat is a contract in restraint of trade within the meaning of the bill . . . [if] customers of the manufacturer are not allowed to sell at a lower rate than that fixed by the manufacturer. . . .

21 Cong. Rec. 4089 (1890) (remarks of Rep. Culberson).

> Even if the conscience of the retailer is touched and he reduces his price[,] the trust steps on him and refuses to sell to him . . . . This monster robs . . . the consumer . . . .

21 Cong. Rec. 4098 (1890) (remarks of Rep. Taylor).

Over the past decades, Congress has often considered the arguments for and against resale price maintenance. Twenty-five years after the Supreme Court held in *Dr. Miles* that resale price maintenance was *per se* illegal, Congress passed the Miller-Tydings Amendment to the Sherman Act, exempting from antitrust illegality certain resale price maintenance agreements in states which adopted so-called Fair Trade laws.[17]

In 1976, Congress responded to the pleas of "President Ford, consumer groups, the Justice Department, the Federal Trade Commission, the Council on Wage and Price Stability, discount stores . . . smaller business associations . . . [and] newspapers across the country" by

[17] 50 Stat. 693 (1937).

enacting the Consumer Goods Pricing Act of 1975.[18] This legislation restored the *per se* illegality of resale price fixing.

The legislative history of the Consumer Goods Pricing Act of 1975 indicates Congress intended to promote price competition at the retail level:

> Some retailers prefer to try to enlarge their share of the market by competing vigorously in price-prescisely (sic) the sort of behavior encouraged by our antitrust laws. This competition is stifled by 'fair trading'.
>
> * * * *
>
> To the extent that the 'Mom and Pop' retailer charges a higher price because he is providing more services to his customers, consumers should have the freedom to choose between paying more for these services and buying nothing but the unadorned product at a lower price from a competitor.

H.R. Rep. No. 341, 94th Cong., 1st Sess. 3, 4 (1975). The Court expressly recognized this legislative purpose shortly thereafter.[19]

Since that time, the Court itself has counselled businesses dissatisfied with the *per se* rule against price fixing to direct their arguments to Congress, rather than the courts.[20] And Congress has spoken on the subject in condemning Executive Branch attempts to overthrow or narrowly interpret the *per se* rule against resale price maintenance. Congress has both re-articulated its views

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[18] Pub. L. No. 94-145, 89 Stat. 801 (1975). S. Rep. No. 466, 94th Cong., 1st Sess. 2 (1975), *reprinted in* 1975 U.S. Code Cong. & Admin. News 1569, 1571.

[19] *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 51 n.18 (1977).

[20] *Arizona v. Maricopa County Medical Society*, 457 U.S. 332, 354-355, (1982). The Court had earlier advised that "Congress [could] ultimately determine . . . [to] make *per se* rules inapplicable in some or all cases." *United States v. Topco Associates, Inc.*, 405 U.S. 596, 610 n.10 (1972).

on the proper reading of Section 1 of the Sherman Act and forbidden the Department of Justice from encouraging the judiciary to modify that reading.

Since 1983, Congress has forbidden the Department of Justice from using appropriated funds to overturn or alter the *per se* illegality rule governing resale price maintenance.[21] Similarly in 1985 when the Justice Department issued Vertical Restraints Guidelines which appeared to countenance all manner of combinations and conspiracies with the purpose and effect of setting resale prices, Congress condemned the Guidelines as inconsistent with the judicial construction and legislative understanding of the antitrust laws.[22]

It is of particular importance that Congress expressly disavowed a statement in the Department of Justice Guidelines that would require proof of the fixing of a specific price as a condition precedent to establishing illegal vertical price fixing:

> The Division claims, again without accompanying authorities, that vertical price fixing is lawful so long as the agreement to fix prices does not set "specific" resale prices and is ancillary to one or more non-price restraints . . . . Such a statement appears to reject or ignore any consideration of the effects of a restraint on price in determining whether there is a price fixing agreement.
>
> * * * *
>
> In all these respects, the Guidelines are inconsistent with existing law and are also demonstrably unsound as a matter of policy.

H.R. Rep. No. 399, 99th Cong., 1st Sess. 14 (1985).

Moreover, in condemning the Guidelines, Congress expressly rejected the requirement of a specific fixed price:

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[21] Pub. L. No. 98-166, § 510, 97 Stat. 1102 (1983); Pub. L. No. 99-180, § 605, 99 Stat. 1169 (1985); Pub. L. No. 99-591, § 605, 100 Stat. 3341-73 (1986).

[22] Pub. L. No. 99-180, § 605, 99 Stat. 1169 (1985).

Whereas such policy guidelines are inconsistent with established antitrust law . . . in stating that vertical restraints that have an impact upon prices are subject to the per se rule of illegality only if there is an 'explicit agreement as to the specific prices;' [and] in stating that restraints imposed by a manufacturer at the request of dealers are vertical in nature and therefore not subject to the per se rule of illegality

* * * *

Now, therefore, be it

Resolved, That it is the sense of the Congress that the antitrust enforcement policy guidelines stated in 'Vertical Restraints Guidelines,' published by the Department of Justice on January 23, 1985—

(1) are not an accurate expression of Federal antitrust laws or of congressional intent with regard to the application of such laws to resale price maintenance and other vertical restraints of trade; [and]

(2) shall not be accorded any force of law or be treated by the courts of the United States as binding or persuasive . . . .

Pub. L. No. 99-180, § 605, 99 Stat. 1169-1170 (1985).

When Congress has so clearly expressed its intent and ratified the judicial construction of a statute, the Court is bound not to overturn that construction precipitously:

> [I]t certainly is 'not for [this Court] to indulge in the business of policymaking in the field of antitrust legislation . . . . Our function ends with the endeavor to ascertain from the words used, construed in the light of the relevant material, what was in fact the intent of Congress.'

Jefferson County Pharmaceutical Ass'n v. Abbott Laboratories, 460 U.S. 150, 170 (1983), *quoting United States v. Cooper Corp.*, 312 U.S. 600, 606 (1941). *See also Illinois Brick Co. v. Illinois*, 431 U.S. 720, 736-737 (1977); *Flood v. Kuhn*, 407 U.S. 258, 284 (1972); *Apex Hosiery Co. v. Leader*, 310 U.S. 469, 488-489 (1940).

III. The Public Interest Is Best Served By Preserving Retail Price Competition

Agreements to eliminate price competition by eliminating competitors should not be sanctioned by this Court: there is no public benefit in allowing a monopolistic dealer to overcharge the public; there is no public benefit in allowing a powerful dealer to bully its suppliers and intimidate its competitors; and there is no public benefit in allowing a manufacturer to coerce its dealers into holding a high, fixed price under the threat of a legalized termination.[23]

The *per se* rule for resale price maintenance is meant to preserve economic freedom of choice and maximize competition. Should millions of individual consumers decide the combination of price and service which best suits their needs? Should the thousands of retailers decide for themselves what price to charge and what profit to earn? Should these retailers strive to make their operations efficient and pass the savings on to consumers? Or should a few manufacturers conspire with their most powerful dealers to dictate the price of all subsequent sales?

Congress answered all these questions when it passed the Consumer Goods Pricing Act of 1975:

> [C]onsumers should have the freedom to choose between paying more for these services and buying nothing but the unadorned product from a competitor.

H.R. Rep. No. 341, 94th Cong., 1st Sess. 4 (1975).

Since "Fair Trade" was abolished in 1975, the retail industry has flourished through innovations and efficiencies which have satisfied actual consumer demand.

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[23] There is certainly no public benefit in allowing a powerful retailer publicly to announce that it will not purchase from suppliers who sell to discounters and to urge that other retailers follow suit. *But see Burlington Coat Factory Warehouse Corp. v. Esprit de Corp.*, 769 F.2d 919 (2d Cir. 1985), *aff'g* 597 F. Supp. 1199 (S.D.N.Y. 1984).

Now, the consumer can freely choose to patronize department stores, specialty shops, discount stores, catalog showrooms or mail order houses, whichever suits the consumer's perceived need for the desired item at the particular time.

In this free market environment, K mart, like Congress, believes that American consumers can determine where they receive the best value for their money. They see "best value" as a combination of the quality of the product, the reputation of the retail store, and the retail price. All else being equal, the lower the retail price, the more consumers will purchase. They spend their money where they perceive the best value; increasingly, they have patronized discount general merchandise stores, such as K mart. It is also K mart's observation that manufacturers (and inefficient retailers) generally tend to believe their products can and should be sold at higher retail prices than the consumers will find acceptable.

The adverse effect of resale price maintenance was proven during the so-called Fair Trade era: wealthy consumers paid significantly higher prices while lower and middle income consumers were foreclosed from purchasing items which they otherwise could have afforded. For example, the Fair Trade laws cost consumers billions of dollars in higher prices.[24] The Department of Justice found that resale price maintenance cost consumers in excess of $2 billion a year in 1975 (when only certain merchandise was "fair traded") and increased retail prices by 18% to 27%.[25] That would mean that K mart shoppers alone could have needlessly paid an additional $4.3 to $6.4 billion in 1986, if manufacturers had been permitted to fix retail prices on all merchandise K mart sold.

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[24] H.R. Rep. No. 341, 94th Cong., 1st Sess. 3-4 (1975); S. Rep. No. 466, 94th Cong., 1st Sess. 3 (1975), *reprinted in* 1975 U.S. Code Cong. & Adm. News 1569, 1572.

[25] S. Rep. No. 466, 94th Cong., 1st Sess. 3 (1975), *reprinted in* 1975 U.S. Code Cong. & Admin. News 1569, 1572.

The most ardent advocates of resale price maintenance often base their arguments on the manufacturer's prerogative to prevent "free-riding," the imagined danger that consumers browse at full-price retailers for product information and services, and then make their purchases from discounters who allegedly offer no such services.[26] These misguided economists, perhaps because they do no shopping themselves, wrongly imagine that full-price retailers always give more service than discounters, or, even more unlikely, that if a manufacturer has forced all retailers to charge a uniform high price, those retailers will necessarily vie for business by some increased sales promotion and service effort.

This is both factually incorrect and theoretically untenable. The fact that full price does not equal full service and that low price does not equal low service is verified by the first-hand experience of consumers on a daily basis and is proved by comparing the level of competition in services during the Fair Trade era with the level which prevails today.[27] And, to the extent that "free-riding" is a problem, Congress itself suggested a far less pernicious and more effective solution than vertical price-fixing:

> [T]he manufacturer could solve this [free-rider] problem by placing a clause in the distributorship contract requiring the retailer to maintain adequate service.

S. Rep. No. 466, 94th Cong., 1st Sess. 3 (1975), *reprinted in* 1975 U.S. Code Cong. & Admin. News 1571.

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[26] K mart spent over $495 million in 1986 on product promotion—and still offered substantial discounts from manufacturer's suggested resale prices and full-price retailers.

[27] Of course, neither full price retailers nor discounters provide significant "service" on most of the consumer goods which were fair traded, such as housewares, clothing and health and beauty aids.

In 1983, the House Committee on Government Operations invited K mart to express its views at oversight hearings on federal antitrust enforcement policy. K mart solicited the opinions of its customers toward manufacturer's vertical price fixing and the retailer's freedom to charge the price it chooses. In a three-week period, consumers sent Congress over one million messages that they cherished their freedom to buy brand name merchandise at discount prices and that they wanted the federal government to stop resale price maintenance.[28] Thus, those who purport to base their defense of resale price maintenance on the welfare of consumers simply ignore the consumers' own perception of their best interests.

Moreover, notwithstanding statements of theory which are either unverified or supported by only the flimsiest of anecdotal evidence, vertical price fixing of the type condoned by the Fifth Circuit stifles efficient and innovative distribution by subsidizing inefficient retailers at the consumers' expense.

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[28] Oversight of Federal Trade Commission Law Enforcement: Fiscal Years 1982 and 1983: Hearings before the Commerce, Consumer and Monetary Affairs Subcomm. of the House Comm. on Government Operations, 98th Cong., 1st Sess. 9 (1983) (statement of Bernard M. Fauber, K mart Chairman and Chief Executive Officer).

CONCLUSION

The judgment of the court of appeals should be reversed.

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No. 85-1910

IN THE

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OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF AMICUS CURIAE OF NATIONAL MASS RETAILING INSTITUTE IN SUPPORT OF PETITIONER

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BRIEF AMICUS CURIAE OF NATIONAL MASS RETAILING INSTITUTE IN SUPPORT OF PETITIONER

INTEREST OF AMICUS CURIAE [1]

The National Mass Retailing Institute ("NMRI") is a nonprofit trade association of mass merchandise retailers. NMRI's 140 members operate over 20,000 retail stores throughout the United States and generate over $126 bil-

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[1] Pursuant to Supreme Court Rule 36.2, both parties to this case—Business Electronics Corporation and Sharp Electronics Corporation—have granted written consents to this filing. Those consents have been filed with the Clerk of the Court.

lion in annual sales. NMRI members range in size from one-store businesses in rural communities to multi-billion dollar chains operating thousands of stores throughout the nation.

Although of diverse sizes, NMRI members share a common marketing approach: mass retailers offer consumers a wide variety of quality products at competitive, discount prices. NMRI members believe that consumers benefit from vigorous retail competition—be it competition among stores selling different products (inter-brand competition) or competition among stores selling the same product (intra-brand competition). In either case, consumers enjoy the lower prices which result from competition. At the same time, NMRI members know that consumers often desire certain services, such as promotional information, point-of-sale instructions, warranty protection, repair capability, or product return policies. NMRI members provide those services. In short, NMRI members strive to offer consumers the desired blend of low prices and needed services. If statistics are any measure, consumers have embraced the industry's marketing approach: mass retailers' sales volume, it has been estimated, has grown over 3400% in the last 25 years.[2]

Above all else, the mass retailing industry owes its success, and its survival, to a retailer's ability to offer brand name products at competitive, discount prices. Mass retailers' operations, as a rule, are marked by high volume sales at low profit margins; prices to consumers are generally well below manufacturers' suggested retail prices. Absent the legal ability to discount, the mass retailing industry could vanish; armed with the right to discount, however, the industry will continue to contribute substantially to the national economy.

NMRI is no stranger to the issues raised in this case. For over a decade, NMRI has labored to preserve the rule

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[2] *True Look at the Discount Industry*, 26 The Discount Merchandiser 37, 43 (1986).

of law that resale price maintenance is illegal *per se*. Mass retailers have sought to protect their right to offer discounts without fear of being terminated by manufacturers, acting in concert with competing dealers which have raised price competition complaints. Over the years, NMRI has testified before Congress, conferred with the executive branch, and participated in litigation, urging the continued retention of the venerable rule of antitrust law that resale price maintenance, in all of its various manifestations, is *per se* illegal.

For example, in 1975, NMRI and others urged Congress to repeal the federal statutes enabling states to enact so-called "fair trade" laws which permitted manufacturers to fix the resale price of brand name goods. These efforts culminated in Congress' enactment of the Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801 (1975) (amending 15 U.S.C. §§ 1, 45(a) (1976)). That Act was tantamount to a codification of the *per se* rule prohibiting resale price maintenance. During the past seven years, as some antitrust enforcement officials have criticized the *per se* rule, NMRI has actively urged Congress to preserve the rule. Congress, in turn, has repeatedly forbidden the antitrust law enforcement agencies from taking steps to change the *per se* rule. NMRI also filed an *amicus* brief in this Court in *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), urging the retention of the *per se* prohibition of resale price maintenance.

In short, because the right to discount is the industry's life blood, NMRI has been and remains active on this important issue. NMRI's views are consistent and straightforward: (1) resale price maintenance is and must remain illegal *per se*; and (2) the *per se* ban applies to conspiracies between manufacturers and higher priced merchants to deny products to lower priced dealers simply because those dealers discount.

This Court's position on this issue has been equally consistent: for over 75 years, the Court has recognized that price fixing is illegal *per se* and, further, that conspiracies to eliminate price competition are included within the *per se* prohibition. Nonetheless, the opinion issued below by the United States Court of Appeals for the Fifth Circuit seeks to erode the *per se* rule by requiring proof not readily found in every "price fixing" case: proof that there was a direct agreement to fix prices "at some level," rather than "merely" proof of a direct agreement to eliminate price competition. This opinion threatens NMRI's members, for it, in effect, sanctions *all* agreements between manufacturers and higher priced retailers to terminate discounters *simply because they are discounters.* To protect the mass retailing industry's hard-earned market position and—more importantly—to preserve consumers' benefits derived from vigorous price competition, NMRI urges the Court to reverse the decision below and to reinstate the jury's verdict. That jury, properly instructed in the law, correctly condemned a conspiracy between Sharp Electronics Corporation ("Sharp") and a higher priced retailer, Hartwell, to terminate petitioner, Business Electronics Corporation ("Business Electronics"), because of its competitive prices.

SUMMARY OF ARGUMENT

The purpose of the Sherman Act is to preserve "free and unfettered competition." *Northern Pac. R. Co. v. United States*, 356 U.S. 1, 4-5 (1958). To accomplish that purpose, this Court and Congress have declared that both intra-brand price and inter-brand price fixing conspiracies are illegal *per se.* This Court and Congress have defined "price fixing" to include a wide variety of practices aimed at eliminating price competition. The present case involves one such practice: the agreement between a higher priced retailer and a manufacturer to eliminate intra-brand competition by eliminating a price cutting

retail competitor as a vendor of the manufacturer's product.

At its simplest level, this case may be only a routine jury instruction case, of importance principally to the litigants. It concerns the propriety of a specific jury instruction in the context of the parties' trial strategies, the evidence presented, and the defendant's seeming acceptance of the notion that the *per se* rule embraces the elimination of price discounting. At that level of analysis, affirmance of the jury's verdict and the trial court's judgment is an easy matter for this Court: the trial court did not grant the particular instruction subsequently mandated by the appellate court for the good and sufficient reason that defendant Sharp, in its entire package of proposed instructions, had not consistently insisted on that instruction.

Rather, Sharp had agreed with plaintiff Business Electronics that, if the *per se* rule was appropriate to any vertical case, it applied to a conspiracy to "eliminate price competition." Indeed, in proposed instruction No. 24, Sharp requested such an instruction. That Sharp did so is hardly surprising—well-settled antitrust jurisprudence has long equated the concerted elimination of price competition, or the concerted elimination of price cutting, with "price fixing." Viewing Sharp's proposed instructions as a whole, Sharp simply did not consistently insist on, and the trial judge thus did not give, an instruction that the jury must find an agreement that prices would be set "at some level." Had the defendant consistently insisted on that instruction, the issue ostensibly before the Court would be more clear-cut: must there be an agreement on resale prices "at some level" to implicate the *per se* rule in vertical price cases?

That issue, while a more substantial public policy issue, can also be easily resolved by this Court. Decades of Congressional findings and judicial rulings on price fixing issues compel a reversal of the decision below. An agree-

ment between a manufacturer and a higher priced retailer to terminate a price cutter, and thereby eliminate price competition, is illegal *per se*. That agreement serves no procompetitive purpose; indeed, it is the antithesis of intra-brand price competition. It is starkly at odds with the mandate of the antitrust laws that there shall be "free and unfettered" price competition, be it inter-brand competition or intra-brand competition. An agreement to eliminate a price cutter allows the complaining dealer, with the manufacturer's approval, to set prices free from competition from the discounter. That agreement produces the same economic effect as if the manufacturer and its dealers were illegally to agree on a specific price for the product. In either case, there is an agreement to eliminate intra-brand price competition between dealers, which will almost always result in higher prices for the product. *See, e.g., California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 102-03 (1980).

Certainly under the jurisprudence of horizontal antitrust cases, agreements to eliminate price competition have always been treated as *per se* illegal "price fixing." For example, the United States has recently brought *criminal* charges against competitors who agreed only to eliminate discount coupons for branded products and did not also agree to set prices "at some level." *United States v. Waldbaum, Inc.*, 1985-2 Trade Cas. (CCH) ¶ 66,689 (D. Conn. 1984).

This Court, too, has long upheld price fixing charges against defendants who sought to defend antitrust charges by denying the existence of an agreement to fix prices "at some level." From *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940) to *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980), this Court has ruled that an agreement to eliminate discounts "falls squarely within the traditional *per se* rule against price fixing." 446 U.S. at 648. It is a very short step—indeed, no step at all—to conclude that, in vertical cases too, an agreement to eliminate discounters also "falls squarely within the traditional *per se* rule against [vertical] price fixing." *Id.* While some may suggest analytical differences between horizontal and vertical *non-price* restraints, there should be no different result in defining what is "price fixing" in a horizontal case and what is "price fixing" in a vertical case. *Midcal*, 445 U.S. at 102-03. Price fixing in either context includes a concerted agreement to eliminate discounts—or discounters. In either context, the effect is the same: higher prices.

Finally, even if there were any further doubt about it, Congress has recently resolved the issue. Within the last two years, Congress declared that a successful prosecution of a vertical price fixing case does *not* depend on proof of an explicit agreement to set specific prices. H.R. Rep. No. 399, 99th Cong., 1st Sess. 14 (1985).

In short, this Court's precedent, Congressional enactments, economic policy, and even the defendant's own package of jury instructions point to one conclusion: conspiracies to eliminate discounters, simply because they are "price cutters," are illegal *per se*.

ARGUMENT

I. A CONSPIRACY TO ELIMINATE PRICE COMPETITION BY TERMINATING A DISCOUNTER IS A *PER SE* VIOLATION OF THE ANTITRUST LAWS

Resale price maintenance is illegal *per se*. This clear rule, although much vilified in certain sectors of academia and under close inspection by lower courts in the past few years, has nonetheless survived. It remains a pillar of antitrust jurisprudence and the source of support for the mass retailing industry and its price-conscious customers. It is a rule which rests on the well-founded premise that intra-brand price competition is good because it enhances consumer welfare. That is, the rule enforces the national judgment that consumers are far better off if vendors are obligated to compete with each other in pricing products

for resale. *See generally Albrecht v. Herald Co.*, 390 U.S. 145, 157 (1968) (Harlan, J., dissenting). First crafted by this Court over 75 years ago and repeatedly ratified and adopted by Congress over the last two decades, the *per se* rule should not be discarded.[3]

The present case requires the Court to reiterate which vertical price agreements are subject to the *per se* rule.[4] Specifically, does the *per se* ban include an agreement to terminate a retailer because its prices are too low—because it is a "price cutter" or "discounter?" The answer is yes: a conspiracy to terminate a vendor because it is a price cutter is *per se* illegal. That answer is drawn from this Court's precedent in both vertical and horizontal cases and Congressional findings and laws in the area. That answer is drawn as well from common sense: a price "cutter" necessarily is one who "cuts" prices below some acceptable level. An agreement to terminate a vendor because it cuts prices necessarily requires some conscious commitment by the manufacturer and a higher priced vendor to a scheme of maintaining higher retail prices. Such an agreement must be condemned as *per se* illegal under the antitrust laws.

A. The *Per Se* Rule In Vertical Pricing Cases: An Overview

Resale price maintenance agreements—that it, agreements to fix or maintain resale prices—were first declared to be illegal by this Court in *Dr. Miles Medical Co. v.*

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[3] *See, e.g., Arizona v. Maricopa County Medical Soc'y*, 457 U.S. 332, 354-55 (1982) ("[A]rguments against application of the *per se* rule in this case therefore are better directed to the Legislature"). *See also Apex Hosiery Co. v. Leader*, 310 U.S. 469, 488-89 (1940).

[4] *See Maricopa County*, 457 U.S. at 361-62 (Powell, J., dissenting) ("It is settled law that once an arrangement has been labeled as 'price fixing' it is to be condemned *per se*. . . . The inquiry in an antitrust case is . . . 'to characterize the challenged conduct as falling within or without that category of behavior to which we apply the label '*per se* price fixing.'' '") (citation omitted).

John D. Park & Sons Co., 220 U.S. 373 (1911). The case involved a manufacturer of proprietary medicines, Dr. Miles, which fixed the prices of its products at both the wholesale and retail level. A wholesale drug concern, John D. Park & Sons, sought to introduce competition into the distribution of Dr. Miles products by buying them at discount prices and selling them at discount prices. Unhappy that its products were being discounted, Dr. Miles sued Parks & Sons for inducing wholesalers and retailers to breach their contracts. This Court upheld the lower courts' decisions dismissing Dr. Miles' complaint. The Court deemed the manufacturer's price fixing agreements to be illegal *per se*, stating that "agreements or combinations between dealers, having for their sole purpose the destruction of competition and the fixing of prices, are injurious to the public interest and void." 220 U.S. at 408.

The ruling in *Dr. Miles*—that resale price fixing is *per se* illegal—has been affirmed by this Court at every subsequent opportunity it has had to discuss the doctrine.[5]

The Court's most recent pronouncement on resale price maintenance, *324 Liquor Corp. v. Duffy*, 107 S.Ct. 720 (1987), involved a New York statute which sought to impose a resale price maintenance scheme on all New York liquor retailers. Noting first that "[r]esale price

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[5] *See United States v. Colgate & Co.*, 250 U.S. 300, 307-08 (1919); *United States v. A. Schrader's Son, Inc.*, 252 U.S. 85, 100 (1920); *FTC v. Beech-Nut Packing Co.*, 257 U.S. 441, 452-53 (1922); *United States v. Line Material Co.*, 333 U.S. 287, 307-08 and n.21 (1948); *Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc.*, 340 U.S. 211, 213 (1951); *United States v. Parke, Davis & Co.*, 362 U.S. 29, 39, 43-44 (1960); *Albrecht v. Herald Co.*, 390 U.S. 145, 151-52 (1968); *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 51 n.18 (1977); *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 102-03 (1980); *Rice v. Norman Williams Co.*, 458 U.S. 654, 659-60 (1982); *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 761 (1984); *324 Liquor Corp. v. Duffy*, 107 S.Ct. 720, 724 (1987).

maintenance has been a *per se* violation of § 1 of the Sherman Act 'since the early years of national antitrust enforcement.'" 107 S.Ct. at 724 (citing *Monsanto*, 465 U.S. at 761), the Court then observed that resale price fixing is illegal because it "prevents manufacturers and wholesalers from allowing or requiring retail price competition." 107 S.Ct. at 724. In short, resale price maintenance was condemned because it prevented "price competition."

This is the common focus of this Court's resale price maintenance jurisprudence: because intra-brand price competition is a desired goal, the *per se* rule applies to those agreements which "prevent price competition. . . ." *Midcal*, 445 U.S. at 103.

Congress, too, has firmly concluded that all resale price maintenance schemes are *per se* violations of the antitrust laws. In 1975, Congress enacted the Consumer Goods Pricing Act and thereby repealed the "fair trade laws" which had authorized states to permit resale price maintenance.[6] This Court subsequently interpreted the Congressional action as an "express[ion] [of Congress'] approval of a *per se* analysis of vertical price restrictions. . . ." *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 51 n.18 (1977). *See Midcal*, 445 U.S. at 102-03. That interpretation is correct, as the legislative history of the Act evidences a clear Congressional endorsement of the *per se* rule.[7]

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[6] Miller-Tydings Act of August 17, 1937, ch. 690, 50 Stat. 693 (amending 15 U.S.C. § 1) (repealed 1975) and McGuire Act of July 14, 1952, ch. 745, §§ 1, 2, 60 Stat. 632 (amending 15 U.S.C. § 45, 45 note) (repealed 1975).

[7] Both the Senate and House Reports on the Consumer Goods Pricing Act provide that resale price maintenance should be illegal *per se*. The Senate Report states:

> This proposed legislation repeals the Miller-Tydings Act which enables the States to enact fair trade laws and the McGuire Act which permits states to enact nonsigner provisions. *Without these exemptions the agreements they authorize would violate the antitrust laws.*

S. Rep. No. 466, 94th Cong., 1st Sess. 1 (1975) (emphasis added) [hereinafter cited as *Senate Report*].

The House Report was even more explicit:

> An agreement between a manufacturer and a retailer that the retailer will not resell the manufacturer's product below a specified price is an abvious [sic] form of price fixing. As such it is *per se* illegal under Section 1 of the Sherman Act.

H.R. Rep. No. 341, 94th Cong., 1st Sess. 2 (1975) [hereinafter cited as *House Report*].

Both the House and Senate sponsors, in explaining the legislation to their colleagues, emphasized that the effect of the Consumer Goods Pricing Act was to subject resale price fixing agreements to the *per se* standard. For example, Rep. Rodino, Chairman of the House Judiciary Committee and the Subcommittee on Monopolies and Commercial Law and a co-sponsor of the bill, stated, while presiding over Subcommittee hearings, that resale price maintenance would be *per se* illegal on passage of the Consumer Goods Pricing Act:

> Agreements, whether vertical or horizontal, to fix and maintain prices are a classic restraint of trade. They have long been considered per se illegal under our antitrust laws.

Hearings on H.R. 2384 Before the Subcomm. on Monopolies and Commercial Law of the House Judiciary Comm., 94th Cong., 1st Sess. 1 (1975) [hereinafter cited as *House Hearings*].

Sen. Brooke, the Senate sponsor of the bill, stated:

> Without these Federal statutes [the Fair Trade laws], these interstate price-fixing conspiracies would be in violation of the most basic of our antitrust laws—the Sherman Antitrust Act and the Federal Trade Commission Act.

121 Cong. Rec. 38,049-50 (1975).

The final proof of the purpose of the Consumer Goods Pricing Act of 1975 is found in the statement of then President Gerald R. Ford who, upon signing the bill, stated that the legislation:

> will make it illegal for manufacturers to fix the prices of consumer products sold by retailers. This new legislation will repeal laws . . . which amended the Federal antitrust laws so

On many subsequent occasions, Congress again declared that resale price maintenance is illegal *per se*. As a recent example, Congress, in appropriations legislation for three

of the last four years, has prohibited the Department of Justice from engaging in any efforts to overturn or alter the *per se* rule. *See* Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriations Act, Pub. L. No. 98-166, § 510, 97 Stat. 1071, 1102-03 (1983); Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriations Act, Pub. L. No. 99-180, § 605, 99 Stat. 1136, 1169-70 (1985); Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriations Act, Pub. L. No. 99-591, § 605, 100 Stat. 3341, 3341-73 (1986).

Even as this brief is filed, Congress continues its efforts to direct the Justice Department to enforce the *per se* rule. *See* H.R. Rep. 2763, 100th Cong., 1st Sess. § 605 (1987); S. 938, 100th Cong., 1st Sess. § 404 (1987); H.R. Rep. No. 182, 100th Cong., 1st Sess. 70 (1987); S. Rep. No. 72, 100th Cong., 1st Sess. 26 (1987).

Congress has not only embraced the *per se* rule, but has defined it to include the concerted elimination of price cutting. In a Report accompanying Congressional enactment of § 605 of Pub. L. No. 99-180, the House of Representatives strongly criticized the "Vertical Restraint Guidelines" issued by the Department of Justice on January 23, 1985 (*See* 1 Trade Reg. Rep. (CCH) No. 687, pt. II, at 1 (Jan. 23, 1985)). H.R. No. 399, 99th Cong., 1st Sess. 14, 16 (1985). The Report concluded that:

> Other "restatements" of law exist in the Guidelines that attempt to dilute or trivialize the generality of the per se rule against price fixing, both horizontal and vertical. The Division claims, again without accompanying authorities, that vertical price fixing is lawful so long as the agreement to fix prices does not set "specific" resale prices and is ancillary to one or more non-price restraints. . . . Such a statement appears to reject or ignore any consideration of the effects of a restraint on price in determining whether there is a price fixing agreement.
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> * * * *
>
> In all these respects, the Guidelines are inconsistent with existing law and are also demonstrably unsound as a matter of policy.

Id.[8]

In sum, Congress continues to emphasize that resale price maintenance—whether it be through the elimination of price cutting or through a direct agreement on specific prices—is illegal *per se*. As has this Court for nearly eighty years, Congress, too, has concluded that intra-brand price competition is a vital goal of antitrust policy. *See Monsanto*, 465 U.S. at 769 (Brennan, J., concurring).

States could authorize otherwise illegal agreements between manufacturers and retailers setting the price at which a product would be sold to consumers.

11 Weekly Comp. Pres. Doc. 1368 (Dec. 12, 1975).

[8] In the legislation condemning the "Vertical Restraint Guidelines," Congress concluded that the "Vertical Restraint Guidelines" did not represent an accurate statement of antitrust law. Congress stated:

> Whereas such policy guidelines are inconsistent with established antitrust law, . . . in stating that vertical restraints that have an impact upon prices are subject to the per se rule of illegality only if there is an 'explicit agreement as to the specific prices'; . . .
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> * * * *
>
> Now, therefore, be it
>
> *Resolved*, That it is the sense of the Congress that the antitrust enforcement policy guidelines stated in "Vertical Restraints Guidelines," published by the Department of Justice on January 23, 1985—
>
> (1) are not an accurate expression of Federal antitrust laws or of congressional intent with regard to the application of such laws to resale price maintenance and other vertical restraints of trade; [and]
>
> (2) shall not be accorded any force of law or be treated by the courts of the United States as binding or persuasive; . . . .

99 Stat. at 1169-70.

B. Resale "Price Fixing" Includes A Conspiracy To Eliminate A Price Cutter

In both vertical and horizontal cases, this Court and lower courts have defined "price fixing" to include the concerted agreement to eliminate *price competition.* In *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940), the Court reviewed an agreement by major oil refiners to participate in a common effort to purchase, and keep off the market, surplus gasoline. The intent was to "stabilize prices." There was no explicit agreement to set prices at some level, only an agreement to take action to stabilize prices. The Court, applying the *per se* rule, concluded:

> Any combination which tampers with price structures is engaged in an unlawful activity. Even though the members of the price-fixing group were in no position to control the market, to the extent they raised, lowered, *or stabilized prices* they would be directly interfering with the free play of market forces. The Act places all such schemes beyond the pale and protects that vital part of our economy against any degree of interference.

310 U.S. at 221 (emphasis added).

More recently, in *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980) this Court, in a *per curiam* opinion, condemned an agreement among beer wholesalers to refuse to extend interest-free credit to retailers. The agreement was not one to fix prices at "some level," but merely an agreement to eliminate what was, in effect, a discount to retailers. The Court, applying the *per se* rule, stated:

> It is virtually self-evident that extending interest-free credit . . . is equivalent to giving a discount. . . . Thus, credit terms must be characterized as an inseparable part of the price. An agreement to terminate the practice of giving credit is thus tantamount to *an agreement to eliminate discounts*, and thus *falls squarely within the traditional per se rule against price fixing.*

446 U.S. at 648 (footnotes omitted) (emphasis added).

In between *Socony* and *Catalano*, this Court similarly condemned a variety of agreements as *per se* unlawful "price fixing" even where there was no explicit agreement on the level of prices. In *FTC v. Cement Inst.*, 333 U.S. 683, 690-93 (1948), the Court invalidated an agreement to use a specific method of quoting prices. In *United States v. Container Corp. of America*, 393 U.S. 333 (1969), the Court prohibited an agreement by which container manufacturers exchanged price information. That agreement, which apparently had the tendency to stabilize prices, was treated as *per se* illegal, as it "chill[ed] the vigor of price competition." *Id.* at 337. According to the majority, "[s]tabilizing prices as well as raising them is within the ban of § 1 of the Sherman Act." *Id.* Justice Marshall's dissent suggested that he would have joined the majority in condemning the agreement if the evidence showed "a deliberate attempt to stabilize prices." *Id.* at 344. That is, all of the Justices seemed to agree that a conspiracy with the purpose of stabilizing prices is illegal even absent an agreement on prices at some level. *See United States v. United States Gypsum Co.*, 438 U.S. 422, 436 n.13 (1978).

All of these cases view unrestrained price competition as the most critical goal of our antitrust laws. These cases reflect the importance of price as the "central nervous system" of our economy. *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679, 692 (1978) (citing *Socony*, 310 U.S. at 226 n.59). Fairly summarized, these cases—admittedly, all arising in a horizontal context—condemn outright concerted agreements which deliberately tamper with the free market determination of price. They condemn agreements which were intended to stabilize prices, or minimize price competition, even if they did not include a commitment to a

particular price or some level of pricing. All of these cases underscore the purpose of the Sherman Act: to preserve "free and unfettered competition." *Northern Pac. R. Co.*, 356 U.S. at 4-5.

The analysis and the result should be no different in vertical cases—there, too, vigorous intra-brand price competition is a critical goal, as evidenced by continued legislative and judicial affirmation of the *per se* prohibition against resale price maintenance. Congress and this Court have, time and time again, declared that intra-brand price competition is an important goal. Thus, application of horizontal price fixing principles in vertical price fixing cases is appropriate and hardly novel. This Court frequently applies horizontal precedent to vertical settings—and vice versa. For example, this Court recently applied conspiracy standards developed in a vertical case to a horizontal antitrust case. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 106 S.Ct. 1348, 1357, 1360, 1362 (1986) (adopting vertical conspiracy standards of *Monsanto*).[9] So, too, should this Court continue to apply the logic and language of horizontal price opinions to vertical price cases. Indeed, one of the underpinnings of the *per se* rule prohibiting resale price fixing is that the practice is akin to horizontal price fixing between retailers. *Dr. Miles*, 220 U.S. at 408; *Midcal*, 445 U.S. at 103.

Following this rationale, an agreement to eliminate discounts—*per se* illegal in a horizontal setting under *Catalano*—is identical to an agreement to eliminate a discounter—illegal under the *Cernuto* line of cases developed in the appellate courts. *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979).[10]

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[9] *See also Kiefer-Stewart*, 340 U.S. at 213-15 (assessing restraint as both horizontal and vertical and applying same analysis).

[10] *See, e.g., Victorian House, Inc. v. Fisher Camuto Corp.*, 769 F.2d 466 (8th Cir. 1985); *Ziddell Explorations, Inc. v. Conval Int'l,*

In fact, the logic of the *Cernuto* line of cases is precisely that of this Court in *Socony* and *Catalano* (*id.* at 169):

> If the purpose and effect of the challenged conduct is to restrain price movement and the free play of market forces, it is then illegal *per se.*

That is, a vertical agreement between a manufacturer and a retailer to stabilize prices by eliminating a price competitor—even if not accompanied by a commitment to an exact price or an exact level—is well within the ambit of the *per se* prohibition of *Dr. Miles* and its progeny. Indeed, one need look no further than this Court's seminal decision in *Monsanto* to verify that conclusion: there, the jury was allowed to find, based in large part on evidence of dealer complaints and retail price "stabilization," that there was a *per se* violation of the antitrust laws. *Monsanto*, 465 U.S. at 768-69 n.14 (discussing evidence of retail price "stabilization" as evidence of a "price-fixing conspiracy."). *See also Albrecht*, 390 U.S. at 149 ("the [*per se* illegal] combination with wholesalers arose because they cooperated in *terminating price-cutting retailers.*") (emphasis added).

The Justice Department, in its brief urging the denial of the writ of certiorari, recognizes the power of the horizontal precedent holding that agreements "to eliminate price competition generally serve[] no procompetitive purpose." Department of Justice Brief to Petition Nos. 85-1910 and 85-2094 for a Writ of Certiorari ("DOJ Br.") at 7. Indeed, even in the last few years when it has re-examined enforcement policies, the Justice Department has brought *criminal* charges against companies accused of interfering with price competition by agreeing to eliminate discounts—even absent an agreement to fix prices at some level. *E.g., United States v. Waldbaum,*

Ltd., 719 F.2d 1465 (9th Cir. 1983). *See also Spray-Rite Service Corp. v. Monsanto Co.*, 684 F.2d 1226, 1234 (7th Cir. 1982), *aff'd on other grounds*, 465 U.S. 752 (1984).

Inc., Crim. No. B-84-51 (D. Conn., indictment filed Aug. 15, 1984). In that case, the Justice Department claimed that an agreement between competing grocery stores to eliminate double coupons was a "price fixing" agreement. That agreement was claimed to be unlawful because it restrained intra-brand price competition between the retailers on those brand name products where manufacturers offered coupons. *See Waldbaum*, 1985-2 Trade Cas. (CCH) ¶ 66,689 (D. Conn. 1984) (sustaining challenge to indictment).

Applying the government's own logic to the present price fixing case compels a comparable conclusion: a concerted agreement by a manufacturer and a higher priced dealer to eliminate brand name product discounts (by terminating a discounter of that product) is illegal because it eliminates price competition.

The Justice Department protests such an application of "horizontal price fixing" precedent to "vertical price fixing" situations by contending that, because some *non-price* vertical restraints may be procompetitive, the Court should "paint[] with a narrower brush," in the vertical field. DOJ Br. at 7. That protest is hollow for several reasons. First, there are also horizontal restraints which are deemed procompetitive, but their existence has not erased the *per se* rule prohibiting naked price fixing. *See, e.g., Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1, 18-23 (1979). The mere existence of some procompetitive restraints has not compelled this Court to eliminate the *per se* rule altogether or to refuse to apply it where the restraint's principal purpose is to restrain price competition. Second, the Justice Department's comments, fairly interpreted, reflect its complete disdain for any *per se* rules in the vertical context (*see Monsanto*, 465 U.S. at 761-62 n.7). That bias, not this Court's precedent, compels the government's suggestion of a "narrower brush." Finally, as the *Cernuto* opinion emphasizes, a conspiracy to eliminate

a discounter, initiated by a higher priced competitor's complaint and desire to avoid price competition at the retail level, cannot be justified as an attempt to promote inter-brand competition at the manufacturer level. *Cernuto*, 595 F.2d at 168.

To be sure, in both horizontal and vertical cases there are lines to be drawn to distinguish *per se* cases from "rule of reason" cases. But, in both areas, the line must be and can be drawn in a way which condemns agreements whose substantial purpose is to stabilize prices by eliminating price competition. In such cases, the probability is extremely high that the consequences are anti-competitive and, as a result, the *per se* rule should apply. *See NCAA v. Board of Regents of Univ. of Okla.*, 468 U.S. 85, 100 (1984). Congress and this Court have repeatedly drawn a line that is transgressed by the court's opinion below. An agreement which has as its purpose the elimination of price discounts—to be distinguished from other vertical agreements which may tolerate *price* competition—is *per se* unlawful.

If further support were required for this proposition, Congress has recently supplied it. Congress recently condemned the Justice Department's "Vertical Restraint Guidelines." In Pub. L. No. 99-180, § 605, 99 Stat. at 1169-70, Congress rejected the Department's Guideline which stated that the *per se* rule against vertical price fixing applies *only* where "[t]here is direct or circumstantial evidence (other than effects on price) establishing an explicit agreement as to the specific prices at which goods or services would be resold." 1 Trade Reg. Rep. (CCH), *supra* p. 12, at 10. Congress rejected that statement: there need not be an explicit agreement on specific prices in order to invoke the *per se* rule. 99 Stat. at 1169-70. Applying that Congressional directive here, the jury's verdict must stand: the agreement between Sharp and a higher priced retailer to eliminate Business Electronics because it was a discounter is illegal price fixing.

II. IN THE CONTEXT OF THE ENTIRE TRIAL, THE JURY INSTRUCTIONS WERE APPROPRIATE

The final reason to affirm this jury verdict—albeit a reason that pales in significance to decades of antitrust precedent and precise Congressional directions on this issue—is derived from defendant Sharp's own package of proffered jury instructions. Among other instructions, Sharp also requested an instruction (No. 24) which required that the jury find an agreement "to eliminate price competition." [11] In so doing, Sharp recognized that

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[11] Defendant's Requested Jury Instruction No. 24: "Necessity of Manufacturer Motive To Fix Prices":

> When a dealer demands that a manufacturer terminate another existing dealer—in effect tells the manufacturer "You must choose between him or me"—even if the dealer is motivated by a desire to eliminate price competition, it is not in and of itself illegal for the manufacturer thereafter to terminate the existing dealer. *Instead, it must be shown that the manufacturer agreed with the complaining dealer to terminate the existing dealer and that, in so agreeing, the manufacturer shared with the complaining dealer the same desire of eliminating price competition for the complaining dealer.*
>
> Thus, for plaintiffs to establish in this case an agreement between Mr. Hartwell and Sharp that unreasonably restrains trade, they must show (1) that Sharp agreed with Mr. Hartwell to terminate plaintiffs' dealership, and (2) not only that Mr. Hartwell was motivated by a desire to eliminate price competition but also that *Sharp was motivated by the same desire to eliminate price competition* for Mr. Hartwell. In other words, even if you conclude that Mr. Hartwell and Sharp agreed that plaintiffs should be terminated and that in making the agreement Mr. Hartwell was motivated by a desire to eliminate price competition, you cannot find an agreement that unreasonably restrains trade unless you also find that *Sharp was motivated by the same desire to eliminate price competition* for Mr. Hartwell. Otherwise, there would be no unity of purpose, or common design and understanding, or meeting of the minds, which is essential to a conspiracy. (emphasis added).

See also Joint Appendix to Petition No. 85-1910 ("JA") at 14-19 (Court's Instructions To The Jury); *Business Electronics Corp. v. Sharp Electronics Corp.*, No. H-78-1020 (S.D. Tex. 1984): Defendant's Motion for Judgment Notwithstanding the Verdict or, in the Alternative, For a New Trial at 2-3, 8; Brief in Support of Defendant's Motion for Judgment Notwithstanding the Verdict, or in the Alternative, For a New Trial at 11-12. Transcript of Proceedings at 1598-99, 1602.

a plaintiff does not need to prove an explicit agreement on resale prices "at some level." In turn, the trial court did not issue the particular instruction subsequently mandated by the appellate court (*i.e.*, proof of agreement to "some level" of prices) for the good and sufficient reason that defendant Sharp had not consistently insisted on that instruction.[12]

Rather, the district court instructed the jury that "[t]he Sherman Act is violated when a seller enters into an agreement or understanding with one of its dealers to terminate another dealer *because of the other dealer's price cutting.*" Joint Appendix to Petition No. 85-1910 ("JA") at 18 (emphasis added).

Subsequently, in its Motion for a New Trial, Sharp affirmed its acceptance of the "elimination of price discounter" instruction. Sharp contended that the trial court "erred in failing to give [Sharp's] Requested Jury In-

---

[12] Sharp did request an instruction that there must be an agreement "to fix or maintain prices of Sharp calculators at a certain level and not just that the agreement may have had some effect on price." Defendant's Requested Jury Instruction No. 23 (JA at 7). That instruction, taken as a whole, was improper for several reasons.

The instruction stated that, "*anytime* a manufacturer terminates a dealer and replaces him with another dealer, or appoints an exclusive dealer [it is] *perfectly legal* under the antitrust laws. . . ." *Id.* (emphasis added). That is a gross misstatement of the antitrust laws. Dealer terminations, if done pursuant to non-price vertical agreements, are subject to a "rule of reason" inquiry of legality—they are not *per se* legal. *E.g., Rice v. Norman Williams Co.*, 458 U.S. 654, 661 (1982).

Moreover, if a dealer is terminated pursuant to a resale price maintenance scheme, that termination is *per se* illegal; it is not "perfectly legal." *E.g., Monsanto*, 465 U.S. at 761, 763.

truction No. 24 to the effect that plaintiff was required to prove that, in terminating its dealership, both Sharp and Hartwell [the complaining dealer] were motivated by the same desire to *eliminate price discounting*." Defendant's Motion for Judgment Notwithstading the Verdict or, in the Alternative, For a New Trial at 8 (emphasis added).

On the critical issue before this Court, then—the need for proof of an agreement on prices "at some level"—Sharp's proposed instruction No. 24 was no different than the one actually given to the jury. Both instructions required the same finding that there had been an agreement to eliminate price competition. The variety of terms used—an elimination of "price competition," or "price discounting," or "price cutting" are synonymous. Thus, in light of the litigants' proposals to the trial court, the trial court did not err in instructing the jury as it did.[13]

In *United States Gypsum Co.*, this Court found the jury instructions regarding participation in a conspiracy, while not as clear as they might have been, nevertheless were "sufficient" and "substantially in accord with those generally given in similar antitrust cases." 438 U.S. at 463. The Court further noted that "in any event, the disputed instruction differed only in minor and immaterial respects from the instruction requested by respondents. *Id.* So too, the disputed instructions in the present case are in accord with those generally given in similar antitrust cases and, in any event, differed in *only* minor and immaterial ways from one of the instructions requested by Sharp. Given the more than ample existence of "price fixing" in this record, the jury's verdict and trial court's judgment should be affirmed.[14]

[13] The actual instructions given to the jury were also in accordance with the now-current ABA model jury instructions for antitrust cases which approve an instruction prohibiting "price stabilization." A.B.A. Sec. Antitrust, Antitrust Civil Jury Instructions at 92-93 (1980 and Supp. 1986). These instructions are also in accord with the *Monsanto* opinion, which, in part, focused its attention on vertical conspiracies which "stabilize resale prices." 465 U.S. at 758 n.2. Price "stabilization," of course, does not require an explicit agreement on prices at some level, but only an agreement to remove price competition and thereby stabilize prices.

[14] We note that the record did show ample evidence that the manufacturer, Sharp, and its high-price customer, Hartwell, did try to fix and stabilize prices at a higher level. Sharp asked Business Electronics ["BEC"] to "clean up [its] pricing structure" and "sought BEC's adherence to the suggested retail price list." Appendix A to Petition No. 85-1910 for Writ of Certiorari by Business Electronics ("App.") at 5a, 15a. Hartwell "complained vigorously" to Sharp about BEC's low prices. *Id.* Hartwell even tried to engage BEC in a price fixing agreement between the two retailers. *Id.* Hartwell "usually" sold the product at Sharp's suggested prices. *Id.* at 6a.

We note also that one of the trial court's instructions did instruct the jury that the case involved "resale price fixing." (JA at 17) ("In determining whether Sharp illegally combined or agreed with another party to fix retail prices. . . .").

In this context—the instructions as a whole, the record evidence, and the defendant's own proposed instruction No. 24—the jury verdict can easily be sustained. Under circuit precedent, it should have been. *Bunch v. Walter*, 673 F.2d 127, 131-32 (5th Cir. 1982).

CONCLUSION

Resale price fixing is illegal *per se*. In order to promote intra-brand price competition, Congress and this Court have repeatedly affirmed this rule. Resale price fixing includes conspiracies to eliminate a discounter. Such conspiracies, aimed at the elimination of intra-brand price competition, deny consumers the benefits of "free and unfettered" price competition. The *per se* rule proscribes the conduct of Sharp and Hartwell in this case. For the above reasons, the decision of the Court of Appeals for the Fifth Circuit should be reversed.

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Supreme Court of the United States

OCTOBER TERM, 1985

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

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No. 85-1910

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1985

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ Of Certiorari To The
United States Court Of Appeals
For The Fifth Circuit

BRIEF OF FORTY-TWO STATES AS AMICI CURIAE IN SUPPORT OF PETITIONER

INTRODUCTION

The States of Alabama, Alaska, Arizona, Arkansas, Colorado, Connecticut, Florida, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New

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Hampshire, New Jersey, New York, North Carolina, Ohio, Oregon, Pennsylvania, Rhode Island, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, Wyoming, and the District of Columbia (hereinafter the "Amici States") submit this brief in support of Petitioner Business Electronics Corporation.

IDENTITY AND INTEREST OF THE AMICI STATES

A. Identity of Amici States

The chief law enforcement officers of the Amici States are charged by law with the duty to enforce their states' antitrust laws, as well as the federal antitrust laws. In addition, they represent their states and political subdivisions in treble damage actions under the federal antitrust laws, and are authorized by law to bring such actions as parens patriae on behalf of the natural citizens of their states.[1/]

1/ 15 U.S.C. § 15c.

B. Interest of the Amici States in This Case

The Amici States, in their capacity as parens patriae, play a major role in federal antitrust enforcement. Moreover, the states' own antitrust laws are generally construed in accordance with federal court decisions interpreting corresponding provisions of the federal laws.[2/] Therefore, the Amici States have a substantial interest in ensuring that federal courts apply the antitrust laws consistently with underlying Congressional policy and with this Court's past decisions.

The Amici States support the contention of Business Electronics Corporation that agreements to

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2/ See, e.g., Marin County Bd. of Realtors v. Palsson, 130 Cal. Rptr. 1, 549 P.2d 833 (1976); People v. North Avenue Furniture & Appliance, 645 P.2d 1291 (Colo. 1982); Neyens v. Roth, 326 N.W.2d 294 (Iowa 1982); Pittsburgh Plate Glass Co. v. Paine & Nixon Co., 234 N.W. 453 (Minn. 1931); State v. Readers Digest Assoc., 81 Wash.2d 259, 501 P.2d 290 (1972); Grams v. Boss, 97 Wis.2d 332, 294 N.W.2d 473 (1980). See also, FLA. STAT. § 542.32 (1985); MD. COM. LAW CODE ANN. § 11-202(a)(2) (1983 Repl. Vol.); UTAH CODE ANN. § 76-10-926 (1979); VA. CODE § 59.1-9.17 (1987).

terminate discounting dealers because of their price cutting should be treated as per se violations of the antitrust laws. This contention is consistent with the Amici States' interest in sound antitrust policy and effective enforcement of the antitrust laws.

SUMMARY OF ARGUMENT

I. Agreements made for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing prices are per se illegal under section 1 of the Sherman Act, 15 U.S.C. § 1. Price is the "central nervous system of the economy" and an agreement that interferes with the setting of price by free market forces is illegal on its face. The critical importance of price competition has led this Court to condemn price fixing agreements, even where the effect upon price may not be direct and immediate. This rule applies to both horizontal and vertical price fixing arrangements.

An agreement to terminate a discounting retailer because of its price cutting has the same pernicious

effect and lack of redeeming virtue as any explicit agreement to set retail prices at a specific level. Such an agreement eliminates price competition among dealers, limits consumer choice, and transfers wealth from consumers to non-discounting retailers. Consequently, per se condemnation of agreements to eliminate price cutters promotes competition by ensuring the viable presence of discounters in the market.

II. A rule of per se illegality for agreements to terminate discounters because of their price cutting will not adversely affect manufacturers' legitimate interest in establishing optimal product distribution systems. Manufacturers may impose reasonable non-price restraints upon their dealers. These restraints may enhance interbrand competition by enabling a manufacturer, through its distribution network, to compete more effectively against other manufacturers.

Further, unless a manufacturer has monopoly power, it may unilaterally impose restraints upon its dealers without antitrust scrutiny. Existing evidentiary rules require proof that tends to exclude the possibility of independent conduct before an agreement may be inferred. Termination of a discounter in response to a competing retailer's complaint is insufficient by itself to support such an inference.

These rules, embodied in Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 356 (1977), United States v. Colgate & Co., 250 U.S. 300 (1919), and Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984), provide manufacturers ample protection against unwarranted antitrust liability. Further, these rules generally provide the manufacturers with considerable flexibility to implement their distribution systems as they see fit. A rule of per se illegality for price fixing agreements, including agreements to terminate discounters because of their price cutting, does not

reduce this flexibility. If a plaintiff successfully overcomes these judicial safeguards, per se treatment of price fixing agreements is fully appropriate.

ARGUMENT

I.

AN AGREEMENT BETWEEN A DEALER AND A MANUFACTURER TO TERMINATE A DISCOUNTING DEALER BECAUSE OF THE DISCOUNTER'S PRICE CUTTING IS ILLEGAL PRICE FIXING.

A. Agreements, Whether Horizontal or Vertical, Which Have as Their Purpose and Effect the Raising, Depressing, Fixing or Stabilizing of Prices Are Per Se Illegal.

Under section 1 of the Sherman Act, 15 U.S.C. § 1, restraints of trade that are inherently anticompetitive and devoid of redeeming virtues "are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use." Northern Pacific Railway Co. v. United States, 356 U.S. 1, 5 (1958). Price fixing is one such trade restraint that has long been held a per se violation of the Sherman Act. Arizona v. Maricopa

County Medical Society, 457 U.S. 332 (1982); United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940).

In Socony-Vacuum, this Court set forth the classic definition of the per se rule against price fixing. The per se rule is not limited to agreements that set prices at some specific level or in a "uniform and inflexible" fashion. 310 U.S. at 222. Instead, "any combination which tampers with price structures" is price fixing. Id. at 221. The per se rule applies to any "combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity . . . ." Id. at 223.

The rationale for the per se ban against price fixing is clear. Price is the "central nervous system of the economy." Id. at 224 n.59. It is generally the most significant aspect of competition and, if eliminated, competition in other areas such as service and product quality may be of relatively little value to consumers.

The critical importance of price competition has led this Court to condemn all combinations that are

formed with the purpose and effect of tampering with prices. Indeed, this Court has expressly rejected the argument that price fixing should be legal if the price fixed is reasonable. United States v. Trenton Potteries Co., 273 U.S. 392 (1927).

The per se prohibition against price fixing is applied to a broad range of practices that do not directly set a specific price. For example, agreements to adhere to previously announced prices and terms of sale, Sugar Institute v. United States, 297 U.S. 553 (1936), agreements to buy surplus gasoline on the spot market to prevent prices from falling, Socony-Vacuum, 310 U.S. 150, and agreements to fix credit terms, Catalano, Inc. v. Target Sales, Inc., 446 U.S. 643 (1980), have all been condemned as per se illegal. The per se rule also applies to agreements to eliminate discounting, id. at 648, and to agreements to exclude discounting dealers from the market. United States v. General Motors Corp., 384 U.S. 127, 147 (1966).

The per se rule against price restraints applies to both horizontal and vertical agreements. This Court held vertical agreements to fix prices to be unlawful in its earliest decision on the issue. Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911). Since then, the Court has consistently applied the per se rule to vertical price fixing. See, e.g., 324 Liquor Corp. v. Duffy, 107 S. Ct. 720 (1987); Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984); Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36, 51 n.18, (1977); United States v. Parke, Davis & Co., 362 U.S. 29 (1960); United States v. Bausch & Lomb Optical Co., 321 U.S. 707 (1944); Federal Trade Commission v. Beech-Nut Packing Co., 257 U.S. 441 (1922). These decisions recognize that vertical price fixing shares the harmful effects and lack of redeeming virtues that characterize other per se unlawful trade restraints. It eliminates intrabrand price competition at the retail level, may facilitate cartelization at the manufacturer level, Sylvania, 433

U.S. at 51, n.18, and replaces competitive pricing with a system where the contours of price competition are set by agreement. Parke, Davis, 362 U.S. at 46-47. The continuing vitality of the per se rule against vertical price fixing is wholly consistent with the Congressional determination that prices should be set by market forces rather than the private agreement of market participants.

Congress explicitly approved application of the per se rule to vertical price fixing by enacting the Consumer Goods Pricing Act of 1975,[3/] which repealed the exemption for state approved price maintenance agreements under the Miller-Tydings and McGuire Acts.[4/] See Sylvania, 433 U.S. at 51 n.18. The legislative history of the Consumer Goods Pricing Act

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3/ Consumer Goods Pricing Act of 1975, Pub. L. No. 94-145, 89 Stat. 801 (amending 15 U.S.C. §§ 1, 45 (a)).

4/ Miller-Tydings Act of 1937, ch. 690, 50 Stat. 693 (1937); McGuire Amendment to the Miller-Tydings Act, ch. 745, 66 Stat. 631 (1952) (both repealed by the Consumer Goods Pricing Act of 1975).

makes it clear that Congress understood that repeal of the Miller-Tydings and McGuire Acts would lead to uniform nationwide application of the per se rule.[5/] In subsequent legislation, Congress reiterated its approval of the per se rule against vertical price fixing.[6/] Congress has also implicitly approved the application of the per se rule by acquiescing in this Court's application of the rule over a period of more than seventy-five years. See Square D Co. v. Niagara Frontier Tariff Bureau, Inc., 106 S. Ct. 1922, 1930-31

5/ See, e.g., H.R. Rep. No. 341, 94th Cong., 1st Sess. 2 (1975); S. Rep. No. 466, 94th Cong., 1st Sess. 1-3 (1975).

6/ See, e.g., Pub. L. No. 98-166, § 510, 97 Stat. 1102 (1983) (prohibiting Department of Justice appropriations for the purpose of altering or overturning the per se rule against vertical price fixing); Departments of Commerce, Justice, and the State, the Judiciary and Related Agencies Appropriations Act, 1986, Pub. L. No. 99-180, § 605, 99 Stat. 1136, 1169 (1985) (same; also criticizes the Department of Justice's Vertical Restraints Guidelines for adopting an overly narrow application of the per se rule).

(1986); Monsanto, 465 U.S. at 769 (Brennan, J., concurring).

B. An Agreement to Terminate a Discounter Because of Its Price Cutting Has the Purpose and Effect of Raising or Stabilizing Prices.

Petitioner, Business Electronics Corporation (BEC), is a former dealer in electronic calculators manufactured by respondent, Sharp Electronics Corporation (Sharp). BEC alleged and proved that Sharp conspired with Gilbert Hartwell, a rival dealer in Sharp calculators, to terminate BEC as a Sharp dealer. The jury's verdict that Sharp had committed a per se violation of section 1 of the Sherman Act was based upon its finding that there was an "agreement or understanding between Sharp and Hartwell to terminate Business Electronics as a Sharp dealer because of Business Electronics' price cutting." Business Electronics Corp. v. Sharp Electronics Corp., 780 F.2d 1212, 1215 (5th Cir. 1986). The primary issue in the court below, and the sole issue presented on this appeal, is whether the agreement found by the jury is

per se unlawful. The court below held that in the absence of an agreement to set prices "at some level," such an agreement must be analyzed under the rule of reason. Business Electronics at 1218.[7/] Because that holding establishes an unwarranted restriction on the scope of the per se rule against vertical price restraints, it should be reversed.

In the context of vertical restraints, it is important to distinguish between price and non-price restraints because the former are per se unlawful while the latter are analyzed under the rule of reason. Monsanto, 465 U.S. at 765. In making that distinction, the substance, purpose, and effect of a

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7/ The court below relied in part upon Monsanto as a basis for this holding. Nothing in the Monsanto ruling, however, requires an explicit resale price maintenance agreement for the per se rule to apply. The sole issue before the Court in Monsanto was whether there was sufficient evidence of agreement, not whether the alleged agreement fell into the category of price or non-price restraints. The Court left the issue of how to distinguish price restrictions from non-price restrictions for another case. Monsanto, 465 U.S. at 759, n.6. The instant case squarely confronts this distinction.

particular restraint determine whether it takes on the character of a "price restraint." Viewed from this perspective, agreements to terminate discounters because of their price cutting plainly fall within the per se rule.

When a manufacturer agrees to a dealer's request to terminate a competing dealer because of the competitor's price cutting, the pernicious effects are readily apparent. The favored dealer "has eliminated the possibility of price competition by the foreclosed dealer." Cernuto, Inc. v. United Cabinet Corp., 595 F.2d 164, 166 (3d Cir. 1979). As a result, the favored dealer will be able to raise or maintain its prices, generating excess dealer profits while reducing output, limiting consumer choice and transferring wealth from consumers to the dealer.[8/] This Court has recognized

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8/ VII P. Areeda, Antitrust Law ¶ 1457 at 167-68 (1986); see Lande, Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged, 34 Hastings L.J. 65 (1982) (arguing that the intent of Congress in passing the Sherman Act was to prevent restraints of trade that (Continued)

the anticompetitive effects of this type of agreement by holding per se unlawful an agreement between a group of dealers and a manufacturer to exclude discounters because of their price cutting. United States v. General Motors Corp., 384 U.S. 127 (1966).

In General Motors, a group of dealers pressured the manufacturer into eliminating discounting dealers, while in the instant case there was only one conspirator at the dealer level. This difference is insignificant. When a manufacturer's decision to terminate a discounting dealer is the product of an agreement with a full price dealer, and prompted by the terminated dealer's pricing policies, "both the purpose and effect of the termination [is] to eliminate competition at the retail level, and not, as in GTE Sylvania, to promote competition at the manufacturer level." Cernuto, 595 F.2d at 168. Moreover, when the decisive motivating factor in the conspiracy is the non-discounting dealer's attempt to eliminate price

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increase prices to consumers).

competition, the agreement is clearly a price restraint. As the court stated in Cernuto,

> It is true that the alleged combination in the case at hand did not set prices at an exact level. But such a traditional conspiracy is not a sine qua non of a per se violation of the Act under the price fixing rubric. If the purpose and effect of the challenged conduct is to restrain price movement and the free play of market forces, it is then illegal per se.

Id. at 168-69.

In the present case, the Fifth Circuit rejected the Cernuto rule and held that an "agreement to terminate a price cutter does not fix prices at any specific or general level but merely frees the complaining dealer to set prices as he chooses." Business Electronics, 780 F.2d at 1216. The court reasoned that such an agreement only indirectly affects price and should be treated as a non-price restriction. Id.

This analysis is fundamentally inconsistent with the well-established definition of price fixing adopted in Socony-Vacuum and its progeny. An agreement to eliminate a discounting dealer is not necessary to

"[free] the complaining dealer to set prices as he chooses." The dealer is already "free" to price as he chooses--he just would rather not price competitively. Such agreements free the complaining dealer to set supra-competitive prices and deprive the discounting dealer of the freedom to set price as he chooses.[9/] As a result, the "freedom" that an agreement to terminate price cutters allows is the freedom to set prices without interference from competitive market forces, the very market regulator central to sound antitrust policy.

The jury rejected Sharp's contention that BEC was terminated for non-price reasons such as free riding or poor sales performance. Business

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9/ This Court has repeatedly emphasized the importance of permitting traders to set prices "in accordance with their own judgment." Arizona v. Maricopa County Medical Society, 457 U.S. 332, 346 (1982) (quoting Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc., 340 U.S. 211, 213 (1951)); California Retail Liquor Dealers Association v. Midcal Aluminum, Inc., 445 U.S. 97, 103 (1980); Parke, Davis 362 U.S. at 46-47.

Electronics, 780 F.2d at 1219. The jury excluded the possibility that any possibly legitimate non-price restrictions were the basis for the termination. Rather, it found that the only purpose of the agreement was to eliminate price competition by BEC. Given that finding, it betrays a "certain unreality," id. at 1218, to contend that the agreement found by the jury was a non-price restraint.

The court below also ignored the crucial distinction, correctly made in Cernuto, between a manufacturer's decision to adopt non-price restraints that may enhance competition on the manufacturer level, and a dealer's use of the manufacturer to eliminate competition on the dealer level. See Cernuto, 595 F.2d at 168-69. The purpose and effect of the latter arrangement is to raise prices and generate excess profits for the dealer, without any redeeming virtue. It therefore deserves per se treatment as much as any explicit resale price maintenance agreement.

The court below stated that it is too difficult for a factfinder to distinguish a termination of a discounter because of its price cutting from a termination of a dealer to improve a manufacturer's distribution scheme. Business Electronics, 780 F.2d at 1217-18. According to the Fifth Circuit, the difficulty in making that distinction could deter manufacturers from structuring their distribution systems as they wish or from acting in response to dealer complaints--choices that Monsanto seeks to protect. Id. at 1217.

Lower courts have not had difficulty distinguishing terminations of dealers based upon non-price restraints from price motivated terminations. In cases where a non-price restriction was violated, dealer terminations have been found legal, even if such terminations were "in response" to price complaints. See, e.g., Morrison v. Murray Biscuit Co., 797 F.2d 1430 (7th Cir. 1986); Terry's Floor Fashions, Inc. v. Burlington Industries, Inc., 763 F.2d 604, 614 (4th Cir. 1985); Moffat v. Lane Co., 594 F. Supp. 45 (D. Mass.

1984). Reversal of the Fifth Circuit's decision in the present case poses no risk that manufacturers will be unable to adopt and enforce non-price restraints that are legitimate under the rule of reason.

The court below also greatly exaggerated the difficulty of distinguishing between price and non-price motivation. Juries can discern a party's motivation from conflicting evidence. Objective evidence will usually be available that relates directly to the issue of price versus non-price motivation. There may be evidence suggesting a non-price purpose, such as evidence that the manufacturer had pre-existing non-price restraints; that the terminated dealer was not promoting the manufacturer's products adequately; that the terminated dealer had a poor payment record; or that the dealer had engaged in fraudulent sales practices. On the other hand, there may be evidence that the asserted non-price motivation was pretextual, such as when the manufacturer sells to dealers that maintain resale

prices but fail to provide desired services, while refusing to sell to dealers that provide the desired services but discount on price. The specifics of the dealer's complaint and the content and timing of the manufacturer's response to the complaint will also often indicate the parties' motivations.

Juries are fully capable of weighing this type of conflicting evidence and arriving at a verdict. As in Monsanto, if the plaintiff alleges that it was terminated for reasons of price and the defendant produces evidence of a non-price motivation, the Court may reasonably place a burden upon the plaintiff to rebut the defendant's asserted justifications.10/ If

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10/ One commentator has suggested that the burden of production could be allocated in the following manner. The dealer must first make a prima facie showing that it was terminated because of its price cutting. The burden of production would then shift to the supplier to show that it terminated the dealer for reasons other than price cutting. The burden would then shift back to the dealer to show additional probative evidence of price motivation, such as supplier assurances to complaining dealers, proof of termination of other price cutters, or failure to terminate non-discounting dealers that engaged in the (Continued)

the plaintiff is unable to produce evidence tending to show that the asserted non-price motivation is pretextual, the per se case could be dismissed on summary judgment or directed verdict. This approach has already been taken in a number of cases. See, e.g., Beach v. Viking Sewing Machine Co., 784 F.2d 746, 750 (6th Cir. 1986) (no agreement where manufacturer's refusal to deal was consistent with its use of exclusive distributorship, policy against transshipping, and service requirements); Terry's Floor Fashions, 763 F.2d at 614 (no agreement where termination consistent with anti-bootlegging policy). To contend that the entire issue must be taken away from juries because in some cases they may reach an incorrect conclusion suggests an unwarranted distrust of the jury system and an unwillingness to permit juries to carry out the

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same practices as the terminated dealer. Jacobson, On Terminating Price-Cutting Distributors in Response to Competitors' Complaints, 49 Brooklyn L. Rev. 677, 707-709 (1983).

tasks given them under the Seventh Amendment of the Constitution.

C. An Agreement to Terminate a Discounter Because of Its Price Cutting Has No Redeeming Virtues.

Only after considerable experience with the anticompetitive effects of a particular business practice will courts classify it as a per se violation of the antitrust laws. For example, in Broadcast Music, Inc. v. Columbia Broadcasting System, 441 U.S. 1 (1979), a blanket licensing arrangement over copyrighted musical compositions was literally "price fixing." However, the Court unanimously agreed that the arrangement had sufficient redeeming value so as to avoid per se condemnation because there was no other practical method for licensees to obtain their deserved fees for the use of their copyrighted music. Similarly, in Sylvania, the Court held that vertical non-price restraints must be analyzed under the rule of reason. Such restraints may achieve certain procompetitive efficiencies because they may be used

by new manufacturers to induce dealer investments, and by established manufacturers to induce retailers to engage in promotional activities or to provide services and repairs without fear of being undercut by "free riders." Sylvania, 433 U.S. at 55.

None of these redeeming virtues is present in the agreement found by the jury in the present case. BEC offered evidence that it was terminated because of its pricing policies. Sharp countered with evidence that it terminated BEC for free riding and poor sales performance. Business Electronics, 780 F.2d at 1219. Weighing the conflicting evidence, the jury dismissed as pretextual Sharp's contentions. Thus, BEC proved that Sharp and Hartwell agreed to terminate BEC because it was discounting, not because it was free riding or violating possibly legitimate non-price restraints.

An agreement merely to terminate a discounter cannot serve a manufacturer's interest in efficient distribution. Ordinarily, a manufacturer will seek to

promote interbrand competition at the retail level so that dealers will sell at optimum prices and in the most efficient manner. See L. Sullivan, Antitrust § 134a (1977). To this end, a manufacturer may try to limit intrabrand competition in order to prevent free riding or to achieve other efficiencies that the manufacturer believes would not occur under a regime of completely unfettered competition. Thus, a manufacturer's interests coincide with consumers' interest in maximum distributional efficiency.

A full price dealer's interests, however, are quite different from those of the manufacturer and consumer. The full price dealer seeks to obtain the highest markup possible and does not necessarily share the manufacturer's interest in an efficient distribution system. Facing competition from more efficient discounters, full price dealers seek affirmatively to prevent or retard the adoption of an efficient

distribution system.[11/] In the absence of aggressive price competition from discounters, full price dealers may abuse local market power derived from lack of consumer information and the high costs of consumer search to extract overcharges.[12/] Thus, when the purpose and effect of an agreement is to protect the full price dealer's interests in eliminating price competition, rather than those of the manufacturer, none of the potentially redeeming virtues identified in Sylvania are present and the per se rule should apply. Cernuto, 595 F.2d at 168.

Application of the per se ban on agreements to terminate discounters because of their price cutting promotes both intrabrand and interbrand competition by providing some measure of protection for discounting retailers. In the absence of a per se rule, powerful full price retailers can coerce manufacturers

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11/ Steiner, The Nature of Vertical Restraints, 30 Antitrust Bull. 143, 171-74 (1985).

12/ Id. at 151.

into cutting off discount retailers.[13/] This would eliminate intrabrand competition between full price and discount retailers, driving up prices, generating excess dealer profits, and transferring wealth from consumers to dealers.

Discount retailers frequently are able to offer lower prices due to their introduction of innovative, highly efficient methods of distribution.[14/] The advantages of these efficiencies will eventually lead to their widespread adoption. However, if powerful but

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13/ For example, in Garment District, Inc. v. Belk Stores Services, Inc., 799 F.2d 905 (4th Cir. 1986), a four hundred store department store chain coerced Jantzen and Puritan Sportswear into halting sales to a discount retailer. Id. at 907. The court's holding that a manufacturer's desire to placate a powerful retailer is a "legitimate, independent" reason for terminating a discounter, id. at 909, is in direct conflict with cases holding that an agreement may arise by coercion. Albrecht v. Herald Co., 390 U.S. 145 (1968); Parke, Davis 362 U.S. at 43. Garment District illustrates the ability of large retailers to coerce manufacturers into adopting restraints that serve retailer rather than manufacturer interests.

14/ See Gerla, Discounters and the Antitrust Laws: Faces Sometimes Should Make Cases, 12 J. Corp. Law 1, 4-5 (1986); Steiner, supra at n.11, 153-55.

less efficient "ull price retailers can freely use their leverage over manufacturers, they may be able to delay or inhibit the introduction of innovative distribution practices. The result may be reduced efficiency and output throughout an entire industry.

Discounting retailers also can enhance interbrand competition. Price pressure from discounters forces competing retailers to seek price concessions from manufacturers.[15/] In many consumer goods industries, retailers carry a number of different brands. As a result, the entire industry feels the pressure for price concessions.[16/] Discounters can also force retail outlets to create private label brands to compete at

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15/ Gerhart, The "Competitive Advantages" Explanation for Intrabrand Restraints: An Antitrust Analysis, 1981 Duke L.J. 417, 426-27 (1981).

16/ Robert Steiner discusses one example of this phenomenon. After the FTC brought a complaint against Levi Strauss & Co., Levi Strauss ended its policy of preventing discounting by resale price maintenance. When discount outlets started a price war on Levi's brand jeans, competing manufacturers dropped their prices and prices for private label jeans also fell. Steiner, supra, 30 Antitrust Bull., at 181-83.

the budget-priced end of the market. See Gerla, supra, 12 J. Corp. Law at 7. Thus, if full price dealers can secure the termination of discounters, the impetus for interbrand competition will decrease.

In sum, agreements by which manufacturers terminate discounters because of price cutting immediately and directly stifle price competition at the retail level. Such agreements may also inhibit the development and use of innovative and efficient distribution practices. Their purposes and effects are identical to those associated with agreements that explicitly set a retail price level, and are therefore per se unlawful.

II.

PROSCRIBING AGREEMENTS TO TERMINATE DISCOUNTERS BECAUSE OF PRICE CUTTING DOES NOT PREVENT MANUFACTURERS FROM MAKING LEGITIMATE BUSINESS DECISIONS.

A. This Court Has Fashioned Rules That Adequately Protect Manufacturers From Unwarranted Antitrust Liability

Manufacturers have a legitimate interest in determining their most effective distribution methods

so that they may vigorously compete with other suppliers. Unless a manufacturer integrates the retailing function with the manufacturing and supply functions, it must rely upon independent business entities to perform the ultimate distribution of its products to consumers. This relationship of manufacturer and retailer typically involves agreements or understandings about how the products are sold at retail--agreements that may restrict the freedom of the retailer. The antitrust laws are designed to ensure that these restrictions do not unreasonably restrain the retailers' trade. However, this Court has been sensitive to the manufacturer's legitimate interest in determining its optimal distribution methods and has fashioned rules to protect that legitimate interest.

As discussed above, this Court has recognized that agreed-upon restraints that are characterized as "non-price restraints" are to be judged under the rule of reason. Continental T.V., Inc. v. GTE Sylvania, Inc.,

433 U.S. 356 (1977). Therefore, under current antitrust jurisprudence, an agreement must be characterized as a "price restraint" before a per se condemnation is invoked. The Court also has long recognized that truly independent manufacturer action is not proscribed by the antitrust laws. Thus, a manufacturer may announce in advance its policy of selling its products only to those retailers who will abide by a particular restraint, even a "price restraint," United States v. Colgate & Co., 250 U.S. 300 (1919), and refuse to deal with those retailers that will not. Additionally, legitimate unilateral conduct cannot be characterized as illegitimate concerted conduct unless evidence is presented that tends to exclude the possibility that a manufacturer and retailer were acting independently. Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984).

Given these rules, once a terminated discounter shows that it was terminated because of its pricing policies and pursuant to concerted action between its

supplier and its competing retailer, per se condemnation of that combination is appropriate. The supplier has received all the benefits of these judicial safeguards and if, despite these protections, a supplier is shown to have agreed with retailers to restrain price competition, application of the per se rule is fully warranted.

B. Manufacturers May Employ Certain Restricted Distribution Arrangements to Enhance Interbrand Competition.

In Sylvania, this Court ruled that non-price vertical agreements would be judged by the "rule of reason."[17/] Faced with a substantially declining market share, Sylvania restructured its ineffective distribution network by limiting the number of dealer franchises in an area and requiring each dealer to sell

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17/ Sylvania explicitly overruled this Court's ruling of only ten years earlier that when a manufacturer sells its product subject to territorial or other restrictions upon resale, a per se violation of the antitrust laws results. United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967).

Sylvania products only from approved locations.[18] Some of the Sylvania dealers that were terminated as a result of this restructuring may have been discounters. However, the fact that discounters are terminated as a by-product of agreements establishing a new distributive scheme does not lead to the conclusion that the agreement was price-related. Rather, Sylvania's bona fide motivation was to improve its poor competitive standing against other manufacturers by inserting location restrictions in its dealer franchise agreements.

The underlying rationale of Sylvania is that a manufacturer has a legitimate interest in determining its most effective distribution methods to compete

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[18] It was not contested that an agreement between supplier and dealer did exist in Sylvania. Footnote 8 to the majority opinion reads:

> Although Sylvania contended in the District Court that its policy was unilaterally enforced, it now concedes that its location restriction involved understandings or agreements with the retailers.

with other manufacturers. Further, manufacturers have a significant stake in the manner by which their dealers sell their products to consumers. Therefore, manufacturers may enter into agreements with dealers specifying, for example, the territories within which or the classes of customers to whom their dealers may sell, the level of promotional activity their dealers must undertake, or a commitment by the dealers to service the manufacturer's products. By these restrictions, manufacturers modify competitive conditions within their distribution network. Although intrabrand competition may diminish, interbrand competition may be enhanced if the manufacturer and its dealers can compete more effectively against the distribution networks of other manufacturers.[19] It is

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[19] See, e.g., Preston, Restrictive Distribution Arrangements: Economic Analysis and Public Policy Standards, 30 Law & Contemp. Prob. 506, 511 (1965).

these possible interbrand benefits that cause vertical non-price agreements to be judged by the antitrust rule of reason.

C. Existing Evidentiary Safeguards Foreclose Finding an Agreement from Ambiguous Circumstances.

In addition to drawing the distinction between price and non-price restrictions, this Court has emphasized the need to distinguish between independent and concerted action in dealer termination cases. See Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752, 760-61 (1984). A non-monopolist manufacturer, for its own business reasons and through the exercise of its independent business discretion, may unilaterally restrain its dealers without implicating the antitrust laws because the requisite element of concerted action is absent.

A manufacturer can announce, before making sales to subsequent resellers of its products, its policy of selling its products only to those who will abide by the restraint (including only to those who will resell at

a suggested price).[20] United States v. Colgate & Co., 250 U.S. 300, 307 (1919). The manufacturer can then unilaterally refuse to make further sales to resellers who, for their independent reasons, choose not to follow the manufacturer's announced restraint. Id. This rule is completely consistent with the proper rationale for permitting some vertical restraints--a manufacturer has a legitimate interest in determining its optimal distribution methods and should be allowed to implement them as long as it does so unilaterally.[21]

20/ Similarly, a retailer can announce its policy not to do business with manufacturers that supply products to discounters. Burlington Coat Factory Warehouse Corp. v. Esprit de Corp, 769 F.2d 919 (2nd Cir. 1985).

21/ Any form of manufacturer-initiated resale pricing program is worthy of heightened scrutiny, due to its intimate relation to that "central nervous system" of the economy--price. The key to the legitimacy of any suggested resale price program is the absolute preservation of resellers' freedom to conduct at all times their business, in their market and subject to their competitive conditions, in whatever manner they deem appropriate, including the freedom to sell at, below, or above the suggested retail price. An agreement, whether express, implied from a course of

(Continued)

Manufacturers and dealers communicate for any number of reasons, however, and these communications are both solicited and unsolicited. Dealers commonly communicate complaints to manufacturers about competing dealers' business practices. These complaints frequently focus on a competing dealer's penchant for undercutting the retail price level and causing the complaining dealer to lose sales. Prior to Monsanto, proof of a dealer termination in response to a competitor's complaints may have been sufficient to support an inference of

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dealing or other circumstances, or imposed through coercion or intimidation, to secure adherence to suggested prices is a per se violation of the Sherman Act. California Retail Liquor Dealers Association v. Midcal Aluminum, Inc., 445 U.S. 97 (1980); United States v. Parke, Davis & Co., 362 U.S. 29 (1960); United States v. Bausch & Lomb Optical Co., 321 U.S. 707 (1944); Federal Trade Commission v. Beech-Nut Packing Co., 257 U.S. 441 (1922); Colgate, 250 U.S. 300 (1919).

concerted action.[22/] To bar a manufacturer from independently effecting the most efficient distribution of its products, solely because the information upon which the manufacturer acts originated as a price complaint, could undermine the manufacturer's ability to implement that distribution scheme.

Therefore, to avoid inhibiting the manufacturer's exercise of its independent business judgment, this Court held that "something more than evidence of complaints was needed."

> There must be evidence that tends to exclude the possibility that the manufacturer and nonterminated distributors were acting independently . . . . [T]he antitrust plaintiff should present direct or circumstantial evidence that reasonably tends to prove that the manufacturer and others 'had a conscious commitment to a common scheme designed to achieve an unlawful objective.'

22/ See, e.g., Bostick Oil Co. v. Michelin Tire Corp., 702 F.2d 1207, 1213-15 (4th Cir. 1983); Spray-Rite Service Corp. v. Monsanto Co., 684 F.2d 1226, 1238 (7th Cir. 1982); Battle v. Lubrizol Corp., 673 F.2d 984, 990-92 (8th Cir. 1982). However, even under the rule of "termination in response to complaints," any inference of concerted action could be rebutted by other evidence.

Monsanto, 465 U.S. at 764 (citations omitted). This rule articulates the Court's belief that "termination in response to complaints" can occur for legitimate business reasons and is too ambiguous a circumstance to permit that fact alone to support a finding of concerted action.[23/]

The court below determined that there was sufficient evidence in the present case to support a jury verdict that concerted action was undertaken.

> There was evidence that, even before Hartwell became a dealer, Sharp sought BEC's adherence to the suggested retail price list. BEC produced evidence tending to show that it was not "free-riding" and that its sales performance was equal to Hartwell's. The logical inferences from such evidence, if drawn by the jury, could support a finding that BEC's termination was not due to the reasons Sharp suggests.
>
> In addition, there was evidence that Hartwell usually followed Sharp's suggested prices. There was also evidence that Hartwell sought to encourage BEC to follow these prices. Finally, the record shows that Hartwell complained vigorously to Sharp about BEC's pricing and that ultimately Sharp responded by terminating BEC. This evidence, taken as a whole and viewed in the light most favorable to BEC, could support an inference that Sharp and Hartwell had agreed that Hartwell would follow Sharp's suggested retail prices and that BEC's termination was pursuant to this agreement.

Business Electronics, 780 F.2d at 1219 (citation omitted).

A rule that an agreement between a manufacturer and a dealer to terminate a discounting dealer because of its price cutting is per se illegal does not undermine Monsanto in the least. A manufacturer may still legitimately act upon dealer complaints without stepping into the forbidden zone of concerted conduct. The court below mistakenly believed that a manufacturer's legal counsel could not fashion a means of safely terminating a discounting retailer if the manufacturer's antitrust liability turned solely on the fact-finder's determination of the manufacturer's motivation. Business Electronics, 780 F.2d at 1218.

23/ The Amici States do not necessarily agree with the Monsanto ruling that "termination in response to complaints" cannot alone permit an inference of concerted conduct. However, as the propriety of the Monsanto rule is not now before this Court, no challenge to that rule is advanced here.

This is decidedly not the case. A manufacturer can, consistent with Monsanto, implement an "automatic" program for "handling" dealer complaints.

Upon receipt of a dealer complaint, the manufacturer can independently investigate the circumstances of the complaint and decide what further unilateral action, if any, to take. At the conclusion of the manufacturer's investigation, it can then communicate to the complaining dealer what actions, if any, it intends to take and, if appropriate, the reasons for those actions. The manufacturer will have stayed within the Colgate and Monsanto boundaries and legitimately protected the integrity of its chosen distribution system. In short, existing judicial rules adequately protect manufacturers and retailers from antitrust liability when proof of concerted activity among them is ambiguous.

III.

CONCLUSION

The Amici States respectfully submit that the decision of the United States Court of Appeals for the Fifth Circuit should be reversed and that the jury verdict in favor of petitioner, Business Electronics Corporation, be reinstated.

DATED: August 21, 1987

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IN THE

[redacted] the United States

[redacted], INC.

Petitioner,

v.

[redacted] ELECTRONICS CORPORATION,

Respondent.

[redacted] TO THE UNITED STATES
[redacted] FOR THE FIFTH CIRCUIT

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QUESTION PRESENTED

Whether a manufacturer may protect its full service dealers and so assure the continued availability of pro-competitive and efficiency-enhancing services by agreeing to terminate free riders?

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No. 85-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE NATIONAL OFFICE MACHINE DEALERS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF RESPONDENT

INTEREST OF THE AMICUS CURIAE

The National Office Machine Dealers Association ("NOMDA") is a national and international organization representing approximately 6500 office machine dealers. It is recognized as a major spokesperson for the business equipment and systems industry. One of NOMDA's principal organizational goals is to strengthen relationships among manufacturers, dealers and end users. NOMDA provides educational and other important services to its member dealers.

As an organization representing many office machine dealers, NOMDA has a substantial interest in this litigation. NOMDA believes that manufacturers should be able to protect their full service dealers in business equipment and systems by terminating free riders on services that full service dealers provide at substantial cost to themselves. This case involves the treatment of this practice under the Sherman Act. Sharp Electronics Corporation ("Sharp") terminated a retailer who was free riding on costly

services provided by a full service dealer. The free rider, Business Electronics Corporation ("BEC"), diverted customers whom the full service dealer had educated about Sharp's product by offering prices that were lower simply because they did not include any element to compensate for the services that had led to the sale.

Many of NOMDA's members sell complex products of the sort that are most efficiently marketed if the dealer offers prospective purchasers a variety of pre-sale, point-of-sale and post-sale services. This Court's decision in the present case will affect the ability of manufacturers to protect their full service dealers in business equipment and systems by agreeing to terminate free riders on such services. Accordingly, NOMDA has a strong interest in the disposition of this case.

STATEMENT

1. In 1973 Sharp terminated BEC as a Houston-area dealer of Sharp electronic calculators. BEC's marketing strategy had been to offer low prices rather than costly pre-sale educational services. Tr. 72-73; 124-128.[1] Because Sharp's calculators were a new and complex product, BEC's focus on low price at the expense of services that were needed to familiarize potential customers with the product was ineffective, and BEC failed to meet Sharp's sales quotas. Defendant's Trial Exhibit No. 26 (introduced and admitted at Tr. 700). Dissatisfied with BEC's sales performance, Sharp appointed a second dealer in the Houston area, Gilbert Hartwell ("Hartwell"), a full service dealer who offered the pre-sale information services and post-sale support that Sharp believed essential to the efficient marketing of its product. Tr. 343-44; 1031; 1102-03.

BEC took this opportunity to dispense with its entire sales force and to free ride on the services Hartwell provided. Once Hartwell had persuaded a customer to buy a Sharp calculator, BEC diverted the sale by circulating a flier advertising the same product for a lower price—a price Hartwell could not match if he was

1. "Tr." refers to the trial transcript.

to recover the cost of providing the services that produced the sale. Tr. 110; 279-280; 283-284; 343-344; 346-348. Hartwell complained about BEC's free riding to Sharp, Pet. App. at 5a-6a, [2] and Sharp eventually terminated BEC in order to prevent its more effective full service dealer from carrying out its threat to cease selling Sharp's product. *Id.* at 6a.

2. BEC then brought suit against Sharp, alleging that it had been terminated because of its price cutting and that the termination was illegal *per se* under section 1 of the Sherman Act, 15 U.S.C. § 1. The district court instructed the jury to find for BEC if Sharp had acted pursuant to an understanding or agreement with Hartwell to terminate BEC because of its price cutting. Pet. App. at 6a-7a. The jury returned a verdict of $600,000 in favor of BEC. The United States Court of Appeals for the Fifth Circuit reversed and remanded, holding that the district court's instruction to the jury had been improper. The court of appeals held that only agreements between a manufacturer and distributor that require the distributor "to set its prices at some level" so that it does not "retain complete freedom to set whatever price it chooses" are illegal *per se* as price fixing agreements. Pet. App. at 13a-14a.

The Fifth Circuit noted the importance under this Court's precedents of distinguishing between agreements to fix prices, which are illegal *per se*, and nonprice agreements such as an agreement to terminate a dealer because of its free riding, which are judged under the rule of reason. Pet. App. at 10a-11a. Because business uncertainty is created by any method of distinguishing these various agreements that depends upon an analysis of the manufacturer's subjective motives, the court adopted a rule that focuses on the content of the agreement and thereby provides meaningful guidance for manufacturers. *Id.* at 12a.

2. "Pet. App." refers to the Petition for Writ of Certiorari which contains the majority and concurring opinions of the court of appeals. These opinions are also reported in *Business Elecs. Corp.* v. *Sharp Elecs. Corp.*, 780 F.2d 1212 (5th Cir. 1986), *cert. granted*, 107 S. Ct. 3182 (1987).

SUMMARY OF ARGUMENT

A.

Because dealers are a key link in the chain of product distribution, the sales practices they adopt greatly affect the competitiveness of the market, manufacturers' sales levels and end user satisfaction with their purchases. Responsible dealers recognize that they benefit manufacturers and end users alike if they offer sales-related services, such as product information. Free riders threaten the provision of such services by depriving more responsible dealers of the sales their services have generated.

NOMDA's motto is "Service and Integrity." Without these two important elements, a dealer does not properly serve its customer. The sale is only one aspect of the transaction. Service and integrity both before and after the sale ensure end user satisfaction. The free rider does not meet these obligations to the customer. It is therefore essential to the efficient operation of the distribution system that manufacturers have the discretion to protect their full service dealers by terminating free riders.

This Court's decisions establish that vertical agreements generally are judged under the Sherman Act pursuant to the rule of reason. A rule of *per se* illegality is applied only in exceptional circumstances, when experience has shown that a type of agreement is always or almost always anticompetitive and without redeeming economic virtues.

This Court has treated as *per se* illegal only those agreements that set the prices a dealer must charge, that is, agreements that restrict a dealer's price flexibility. Any extension of the scope of the *per se* rule beyond such agreements must depend on a showing that a type of agreement is almost invariably anticompetitive. Economic analysis demonstrates, however, that agreements to terminate free riders enhance marketing efficiency and stimulate intrabrand and interbrand competition.

B.

Efficient marketing of many products requires that dealers provide pre-sale, point-of-sale and post-sale services. For example, new or complex products must be promoted with point-of-sale information services. Dealers have no incentive to offer costly services unless they enhance marketing efficiency and satisfy consumer preferences.

Dealers who provide services must recapture their cost in the price at which they sell. This leaves full service dealers subject to free riding by dealers who do not provide services themselves. Free riders divert customers whom full service dealers have educated about a product by offering the product at a lower price. If free riders operate in a market, soon no dealer will find it worthwhile to offer costly (but efficient) services. Dealers will cease to offer services in order to be able to compete on price terms with the free riders. Free riding therefore jeopardizes the provision of efficiency-enhancing sales-related services. One way a manufacturer can protect its full service dealers and assure the continued provision of needed services is by restricting dealer locations, a practice to which this Court applied the rule of reason in *Continental T.V., Inc.* v. *GTE Sylvania Inc.*, 433 U.S. 36 (1977). Another method of achieving exactly the same result is to terminate free riders.

Agreements to terminate a free rider promote interbrand competition. They induce investment in the provision of services necessary to the efficient marketing of many products, thus permitting manufacturers to compete more effectively. Any price increases that may result indirectly from the termination of free riders are pro-competitive, since they enable dealers to offer services that stimulate interbrand competition.

The termination of free riders also encourages intrabrand competition, as dealers compete on nonprice terms by providing better services. Alternatively, dealers who can offer services at lower cost may be able to shade their prices, thereby engaging in an efficient form of intrabrand price competition.

Because an agreement to terminate a free rider enhances marketing efficiency by ensuring that the optimum level of sales-related services is provided, and because it promotes interbrand and intrabrand competition, it has none of the economic characteristics that have led this Court to hold restraints of trade unlawful *per se*. An agreement to terminate a free rider is a nonprice restriction, properly judged under the rule of reason.

ARGUMENT

THE LEGALITY OF AN AGREEMENT TO TERMINATE A FREE RIDING RETAILER SHOULD BE JUDGED BY THE RULE OF REASON

Dealers are a key link in the chain of product distribution. Vigorous competition in the marketplace, manufacturers' success in marketing their products, and end users' satisfaction with their purchases all depend on the sales practices dealers adopt. Responsible dealers recognize that their role begins before, and continues after, a sale is made. They recognize that they generate more sales and give customers greater satisfaction if they educate potential purchasers about products prior to making a sale and provide repair and other services afterwards. Dealers are hamstrung in their efforts to provide these beneficial services by free riders, who offer no services themselves. Instead, free riders divert buyers who have taken advantage of another dealer's services, offering prices that are lower because they do not reflect the true cost of making the sale. By depriving dealers of sales generated by services offered at significant cost to themselves, free riders threaten the continued provision of services, and hence the efficient operation of the distribution system. Responsible dealers are therefore rightly concerned about free riding, and about preserving the discretion of manufacturers to protect full service dealers by terminating free riders.

Petitioner BEC and its supporting *amici* have presented an argument to this Court that simply begs the question. They label the conduct of respondent Sharp as "price fixing" and then proceed to cite long lists of cases that condemn price fixing as illegal

per se. That sterile exercise in labeling is out of harmony with this Court's recent decisions. These decisions make it clear that *per se* rules should *not* be applied absent a careful analysis demonstrating that the practice at issue is always or almost always injurious to competition and economic efficiency. Analysis of the effects of terminating free riding retailers clearly shows that such terminations promote efficient and vigorous competition in the marketplace. If accepted, petitioner's sweeping expansion of the *per se* prohibition against price fixing would seriously undermine efficiency in product distribution to the ultimate detriment of the American end user.

A. Determining Whether An Agreement Is To Be Judged Illegal *Per Se* Or Analyzed Under The Rule Of Reason Requires Careful Consideration Of Its Economic Effects.

This case brings into focus the basic economic fact that dealers cannot offer sales-related services—even though they promote competition, increase sales and end user welfare—unless dealers can recover the cost of providing those services in the prices they charge. Free riders threaten a dealer's ability to recover the cost of services provided and hence the continued provision of services. Free riders divert customers by offering prices that are lower simply because they include no element of compensation for the services that persuaded the customer to buy. Competing dealers are forced to stop offering costly services so that they can match the free riders' prices, or to stop distributing the affected product altogether.

When Sharp terminated BEC as a dealer in electronic calculators, it eliminated a retailer who was free riding on another dealer's investment in services. It did so, moreover, in a situation where the full service dealer, Gilbert Hartwell, had made it plain that continued free riding would force him to stop carrying Sharp's calculators, leaving Sharp with *no* Houston area dealer to provide information and services needed for the efficient and competitive marketing of Sharp's new and complex product. BEC nevertheless claims that the alleged agreement between

Sharp and Hartwell that Sharp would protect its full service dealer by terminating BEC was a *per se* illegal price fixing agreement under section 1 of the Sherman Act, 15 U.S.C. § 1.

This Court's prior cases, however, have established "the 'rule of reason' as the prevailing standard of analysis" under section 1 of the Sherman Act. *Continental T.V., Inc.* v. *GTE Sylvania Inc.*, 433 U.S. 36, 49 (1977). A court applying the rule of reason considers all the effects of a particular agreement before ruling that it should be prohibited because its net effect is to "suppress or even destroy competition." *Chicago Board of Trade* v. *United States*, 246 U.S. 231, 238 (1918). This favored rule of reason analysis gives way to the application of *per se* rules of illegality only in exceptional circumstances, where experience shows that a practice has such a "pernicious effect on competition and lack of any redeeming virtue," *Northern Pacific Railway* v. *United States*, 356 U.S. 1, 5 (1958), that instances of the practice that do not have an anticompetitive effect "are not sufficiently common or important to justify the time and expense necessary to identify them." *Sylvania*, 433 U.S. at 50 n.16. *See also Broadcast Music, Inc.* v. *Columbia Broadcasting System*, 441 U.S. 1, 19-20 (1979) (in determining if the *per se* rule applies, the Court's inquiry "must focus on whether the effect and . . . purpose of the practice are to threaten the proper operation of our predominantly free-market economy—that is, whether the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output . . . or instead one designed to 'increase economic efficiency and render markets more, rather than less, competitive'").

BEC argues that an agreement between a manufacturer and dealer that a free riding dealer should be terminated is one of the narrow group of practices that this Court has determined under the *Northern Pacific* standard to be *per se* illegal. BEC's argument proceeds by simply labeling such an agreement "price fixing," and then pointing out that price fixing has been considered *per se* illegal since *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U.S. 373 (1911). This Court, however, has refused to

decide antitrust cases by affixing simplistic labels to practices with complex economic effects. *See Broadcast Music, Inc.*, 441 U.S. at 8-9. It engages, rather, in a "functional antitrust analysis," focusing on the economic consequences of a practice. *Sylvania*, 433 U.S. at 46-47. Only such an analysis can show whether a given agreement or type of agreement is properly condemned on a *per se* basis. *Id.* at 58-59 ("departure from the rule-of-reason standard must be based upon demonstrable economic effect"). *See also* Phillips & Mahoney, *Unreasonable Rules and Rules of Reason: Economic Aspects of Vertical Price-Fixing*, 30 ANTITRUST BULL. 99, 101 (1985). Analyzing the function and economic effects of an agreement to terminate a free rider demonstrates that they are very different from the function and effects of vertical agreements this Court has held to be illegal *per se*; the label BEC attempts to attach to Sharp's alleged agreement with Hartwell is a totally inappropriate one.

This Court's past cases have treated as *per se* illegal only those agreements that set the prices a dealer must charge, that is, agreements that restrict a dealer's flexibility in deciding what prices to charge.[3] In *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752, 761 (1984), this Court noted the "important distinction in distributor-termination cases . . . between concerted action to set prices and concerted action on nonprice restrictions," stating that only the former are illegal *per se* while the latter are judged under the rule of reason. The evil addressed by the rule prohibiting vertical price fixing—as the term itself denotes—is the distributor's agreement that it will "conform[] to the [manufacturer's] suggested price," *id.* at 764 n.9, so that the distributor is "not making independent pricing decisions." *Id.* at 762.

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3. Contrary to BEC's contention, BEC Br. at 36-38, congressional criticism of the Vertical Restraints Guidelines issued by the Department of Justice, *see* Pub. L. No. 99-180, § 605, 99 Stat. 1136, 1169-70 (1985), does not undercut this view of the scope of the *per se* rule against price fixing. As the Government noted in its amicus brief at the the certiorari stage in this case, U.S. Br. at 11 n.12, congressional criticism was apparently directed not at the Justice Department's view of the scope of the rule, but at its view of the evidence necessary to prove an agreement to fix prices. Congress has not, of course, amended the antitrust laws to embody this criticism.

Thus, in *United States* v. *Colgate & Co.*, 250 U.S. 300, 307 (1919), the Court quashed an indictment that failed to charge Colgate "with selling its products to dealers under agreements which obligated the latter not to resell except at prices fixed by the company." *See also Albrecht* v. *Herald Co.*, 390 U.S. 145, 150 (1968) (striking down a combination to force retailers "to conform to the advertised price"); *United States* v. *Parke, Davis & Co.*, 362 U.S. 29, 46 (1960) (striking down a "program to effectuate . . . retailers' adherence to . . . suggested retail prices"); *United States* v. *A. Schrader's Son, Inc.*, 252 U.S. 85, 99 (1920) (noting the "obvious difference" between a manufacturer indicating his wishes concerning prices and an agreement binding dealers "to observe fixed resale prices").

The limitation of the *per se* rule against vertical price fixing agreements to those agreements that restrict dealer price flexibility is an inevitable consequence of this Court's focus on the economic effects of vertical agreements. As we demonstrate below, economic analysis shows that, like the dealer location agreements to which the Court applied the rule of reason in *Sylvania*, agreements to terminate free riders have substantial beneficial economic effects, enhancing efficiency in a number of ways. Far from restraining competition, such practices stimulate nonprice competition without restricting dealers' ability to compete efficiently on price terms.

B. Termination Of Free Riders Improves Efficiency By Ensuring The Continued Provision Of Essential Sales-Related Services.

The economic substance of agreements to terminate free riders is that they are nonprice restrictions on the way retailers market a manufacturer's products. Such agreements help manufacturers ensure the efficiency of their distribution systems by guaranteeing that sales-increasing services will be provided by dealers; they protect dealers' investments in the provision of services from free riders; and they benefit end users by ensuring the availability of services needed to make informed purchasing decisions.

1. *Pre-Sale Educational Services.* The sales process is not usually complete with a simple sale. The efficient marketing of many products requires that dealers provide services, both before and after the sale. Before a sale, full service dealers provide information about a product; after a sale, they stand behind the products they carry, providing repair facilities and information support.

Dealers offering pre-sale informational services educate potential purchasers about a product's qualities and capabilities and explore with end users the fitness of the product for particular purposes. The need for dealers to promote products through pre-sale informational services is particularly acute in the case of complex items such as computers, business equipment and systems, household electronic goods, and video or audio equipment. The electronic calculators manufactured by Sharp in 1973 fall into this category. End users could not appreciate the advantages of particular products of this type and could not make informed purchasing decisions unless they receive specialized information. Tr. 113-14; 343-46; 1429-39.

Pre-sale information services are also particularly necessary for the products of a new market entrant, and for new products in general. New products, unfamiliar to the mass of end users, must be introduced to them and their advantages explained, if the product is to gain end user acceptance. *See* Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86, 95 (1960).[4] Beyond these special cases, *any* product with characteristics the end user cannot readily evaluate through simple

4. FTC-sponsored studies of the impact of vertical restraints have found protection of dealers from intrabrand competition so important in these situations that the FTC concluded that even resale price maintenance—price fixing—"was beneficial for consumers and for society as a whole when used early in the product's life cycle and when used by new [market] entrants." FTC BUREAU OF ECONOMICS, "Introduction and Overview," in *Impact Evaluations of Federal Trade Commission Vertical Restraints Cases* 1, 30 (R. Lafferty, R. Lande & J. Kirkwood, eds., 1984). This Court in *Sylvania* also noted that one of the ways in which manufacturers entering new markets could use vertical restrictions in order "to compete more effectively against other manufacturers" was to apply restrictions "to induce competent and aggressive retailers to make

(footnote continued on following page)

examination will be more effectively marketed if the dealer offers services to educate the end user about the product.

Pre-sale information services have efficiency effects beyond promoting sales. End users benefit directly from such services because they increase the likelihood that end users will purchase products that meet their requirements. End users also benefit indirectly because the services promote efficient distribution, thus reducing distribution costs that are included in the purchase price. The general allocative efficiency of the economy also is furthered; the choices informed end users make translate into profits or losses for manufacturers, with the net result that manufacturing output tends to move towards products that informed end users desire. *See* R. BORK, THE ANTITRUST PARADOX at 91 n.* (1978).

Pre-sale services will not be provided except when these beneficial effects are expected to follow. If the provision of services does not "increase the demand for a manufacturer's product more than enough to offset any reduction in demand resulting from the higher distribution margin necessary to compensate for them . . . they generally will not be provided." Cady, *Reasonable Rules and Rules of Reason: Vertical Restrictions on Distributors*, 46 J. MARKETING 27, 31 (1982). Furthermore, the services, if offered, can safely be assumed to satisfy consumer preferences, for "[a] manufacturer has no incentive to provide service for which the utility to the consumer does not equal or exceed the cost of providing it, since to do so would simply reduce demand for the manufacturer's product." *Id.*

Detailed information is usually provided most effectively by the dealer. "The more detailed the information, the more efficient it will be to provide it at the point of sale to persons who have identified themselves as potential buyers and who . . . may have questions not easily anticipated and addressed in mass market advertising." Bork, *Vertical Restraints: Schwinn Overruled*,

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(footnote continued from previous page)
the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer." *Sylvania*, 433 U.S. at 55.

1977 SUP. CT. REV. 171, 181 (1977). But the dealer must make a significant investment if he is to provide this service. He must hire trained sales staff and frequently, because it takes time to impart information to customers, hire more staff than would otherwise be necessary. The dealer will need demonstration models and personnel trained to operate and explain them. He may also engage in local advertising. Part of the information package offered by the dealer will include displaying a full range of a manufacturer's products, requiring ample (and hence costly) display space. *Id.*

2. *The Free Riding Phenomenon.* A dealer who provides these efficiency-enhancing pre-sale services must recapture their cost in the price at which the dealer sells. *See Monsanto*, 465 U.S. at 762-763; Bork, *Vertical Restraints: Schwinn Overruled*, 1977 SUP. CT. REV. at 181. For this very reason, full service dealers are subject to free riding by dealers who do not provide services themselves and so can sell the same products for less. "[S]ome dealers will perceive that they can let others incur the costs of persuasion and capture the customer by offering a lower price. Such dealers take a free ride." Bork, *Vertical Restraints: Schwinn Overruled*, 1977 SUP. CT. REV. at 181. The customer in this situation "has an incentive to absorb the information [offered by the full service dealer] and then to decamp for the nearest discount store and purchase the same article at a price not incorporating its cost of provision." Caves, "Vertical Restraints As Integration By Contract: Evidence And Policy Implications," in *Impact Evaluations, of Federal Trade Commission Vertical Restraints Cases* 429, 433 (R. Lafferty, R. Lande & J. Kirkwood, eds., 1984).

Customer benefits stemming from the presence of free riders—getting both the information and low price that they want—are short lived. If free riders undercut full service dealers, soon no dealer finds it worthwhile to offer costly pre-sale, point-of-sale and post-sale services. These services will simply disappear as dealers become unable to afford to provide them.

See T. OVERSTREET, RESALE PRICE MAINTENANCE: ECONOMIC THEORIES AND EMPIRICAL EVIDENCE at 49 (FTC Bureau of Economics Report 1983) (free riding causes "the unfettered market to underprovide valuable services or not to provide them at all"). "This situation reduces consumer welfare since desired services cannot be obtained. It reduces manufacturers' [and dealers'] welfare because sales revenue and profit are reduced." Cady, *Reasonable Rules and Rules of Reason: Vertical Restrictions on Distributors*, 46 J. MARKETING at 31.

Of course, free riding also jeopardizes the other benefits noted above that result from the provision of sale services. The development of new products, for example, may be deterred. This occurs because pre-sale services are essential to creating a market for new producers and products. If a competing dealer is able to free ride on expensive market development services offered by a full service dealer, manufacturers may find it difficult to persuade *any* dealer to offer those services. "A distributor will refrain from making the required initial investment [in promotion and market development] if there is a reasonable probability that a competitor can benefit from its market development activities before the costs of undertaking those efforts have been recouped and normal returns obtained." *Id.* at 32. It follows that free riding may have the anticompetitive effect of chilling the marketing, and hence the development and manufacture, of new products.

To "evoke the optimal level of dealer presale services" manufacturers must be able to protect full service dealers from competing free riders. Posner, *The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision*, 45 U. CHI. L. REV. 1, 6 (1977). Manufacturers must be able to assure "dealers that the fruits of product-connected services they provide [cannot be] usurped by cut-rate, no-frills competitors." Marvel, *Exclusive Dealing*, 25 J.L. & ECON. 1, 2 (1982).

3. *Protection of Full Service Dealers.* One way to protect a full service dealer from unfair intrabrand competition from free riders is for a manufacturer to limit the number and location of

retailers of its products, a method held in *Sylvania* to be subject to the rule of reason test. Another method, however, is for the manufacturer to terminate dealers who free ride. The termination of free riders, just like the restriction of dealer locations in *Sylvania*, eradicates inefficient intrabrand competition that threatens to curtail the optimum level of service. Indeed, this Court explicitly recognized in *Sylvania* that the vertical restriction there in issue was one way the manufacturer could attempt to overcome free riding that endangered optimum service levels. As the Court stated, "[b]ecause of market imperfections such as the so-called 'free rider' effect, [services that promote efficiency] might not be provided by retailers in a purely competitive situation." *Sylvania*, 433 U.S. at 55. To draw a distinction for Sherman Act purposes between the dealer location and dealer termination methods of counteracting free riding would be to make a distinction "essentially unrelated to any relevant economic impact"—the very ground upon which the *Sylvania* Court found *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), to be defective. *Sylvania*, 433 U.S. at 56.

The present case exemplifies the free riding problem described above and acknowledged in *Sylvania*. Sharp's new, complex and unfamiliar product competed with electro-mechanical calculators that had an established market. Tr. 356; 358-59. Sharp could only succeed in the face of this competition if its dealers educated potential buyers about their product by offering extensive pre-sale services. The record shows the substantial amount of informational services that were required: a dealer usually had to make four or five sales calls on a customer before that customer bought a Sharp calculator. Tr. 113-114; 343-348; 1429-1432. BEC did not provide these pre-sale services. Tr. 72-73; 124-128. Inevitably, BEC's sales of Sharp calculators were much lower than Sharp desired. *See* Defendant's Trial Exhibit No. 26 (introduced and admitted at Tr. 700).

Hartwell, on the other hand, was a full service dealer. He offered the sort of services necessary to stimulate demand for Sharp's new product through his trained sales staff. Tr. 343-344;

1031; 1102-1103. In this classic free rider situation, BEC dispensed with its sales force, stopped advertising, and diverted prospective buyers whom Hartwell had given costly education by circulating fliers offering the same products at prices that were lower—precisely because BEC did not need to pay for pre-sale services. Tr. 110; 279-280; 283-284; 343-344; 346-348. Of course, Hartwell could not compete in this situation and so advised Sharp. Sharp therefore was compelled to act decisively to assure that the services necessary to market its product would continue to be offered to consumers. Its termination of BEC was a rational, efficiency-enhancing, and pro-competitive response to protect its full service dealer from unfair competition from BEC that was disrupting Sharp's marketing strategy.[5]

C. Termination Of Free Riders Prevents An Inefficient Form Of Marketing While Promoting Vigorous Competition.

Conduct is held *per se* illegal under section 1 of the Sherman Act only when it is "manifestly anticompetitive." *Sylvania*, 433 U.S. at 50. The termination of free riders, however, as shown above, eradicates an *inefficient* form of competition—competition that relies on the provision of services by another dealer and so endangers the continued availability of those efficiency-enhancing services. It does not, however, reduce *efficient* forms of competition.

1. *Interbrand Competition.* In determining what vertical restraints are *per se* illegal, this Court has paid special attention to the effect of those restraints on interbrand competition. *See*

5. Dealers may offer many other services, in addition to pre-sale information, that expose them to free riding. One of the most important is repair service that cannot be priced at full cost. *See* Caves, "Vertical Restraints as Integration by Contract: Evidence and Policy Implications," in *Impact Evaluations of Federal Trade Commission Vertical Restraints Cases* at 433-34. Another is the projection of an image of quality for products carried, through shopping environment, sales methods, refund policies and other services. *See* T. OVERSTREET, RESALE PRICE MAINTENANCE: ECONOMIC THEORIES AND EMPIRICAL EVIDENCE at 56-58. Customer support in the form of technical information and problem-solving techniques also, in NOMDA's experience, exposes dealers to free riding.

Sylvania, 433 U.S. at 51-57 (relying on the increase in interbrand competition created by dealer location restrictions); Posner, *The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision*, 45 U. CHI. L. REV. at 5 (in *Sylvania*, the Court endorsed "the primacy of interbrand competition" in the analysis of vertical restraints).

Agreements to terminate a free rider promote interbrand competition. Just like the dealer location restrictions in *Sylvania*, termination of free riders permits a manufacturer "to compete more effectively against other manufacturers." *Sylvania*, 433 U.S. at 55. By terminating free riders, a manufacturer of new products can "induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer." *Id.* And "[e]stablished manufacturers can ... induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products." *Id.*

Furthermore, the classical explanation for the potential anticompetitive interbrand effect of vertical price fixing has no application in the case of the termination of a free rider. Vertical price fixing has been said to be anticompetitive because it facilitates horizontal cartelization at the manufacturer level by easing the burden of cartel policing: fixed prices "enhance[] the likelihood of detecting manufacturer price shading," i.e., cheating on the cartel. T. OVERSTREET, RESALE PRICE MAINTENANCE: ECONOMIC THEORIES AND EMPIRICAL EVIDENCE at 21 (emphasis omitted). *See also* Marvel & McCafferty, *The Welfare Effects of Resale Price Maintenance*, 28 J. L. & ECON. 363, 365 (1985). An agreement to terminate a free rider can have no such detrimental effect on interbrand competition. Absent a separate agreement to reduce dealer price flexibility, an agreement that a free rider should be terminated leaves remaining dealers free to follow the manufacturer's recommended retail prices or not, as the dealers see fit—a fact illustrated in this case, where Hartwell did not always follow Sharp's suggested retail

prices, and did not believe himself to be obligated to sell Sharp's calculators at any particular price. Pet. App. at 6a. The dealer who is a party to the agreement is free to vary its prices in response to market conditions including, most obviously, competition from other products.

Moreover, termination of a free rider in no way gives full service dealers free rein to raise prices. Interbrand competition remains a potent disincentive to raising prices; and interbrand competition will continue after the elimination of free riders to keep profit margins low. *See* Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6, 16 (1981).

It is clearly not enough to condemn an agreement to terminate a free rider that one of its indirect effects may be to enable remaining retailers to raise their prices within limits imposed by interbrand competition. First, any price increases that indirectly result from such an agreement are actually pro-competitive, since they enable dealers to offer the very services that, as this Court noted in *Sylvania*, stimulate interbrand competition. Relieved of pressure from free riders continually undercutting a dealer, that dealer may increase its prices to the level necessary to provide customers with the mix of information and services that the dealer and manufacturer believe will result in the most effective distribution.

Second, any expansive definition of "price fixing" to include agreements potentially having an indirect impact on prices would be "flatly inconsistent with *Sylvania*," because, as the court of appeals in this case recognized, *see* Pet. App. at 9a, "[v]irtually all of the justifications for vertical nonprice restrictions endorsed in *Sylvania* assume an indirect effect on price." *See generally* Baker, *Interconnected Problems of Doctrine and Economics in the Section One Labyrinth: Is Sylvania a Way Out?*, 67 VA. L. REV. 1457, 1467 (1981). *Accord* T. OVERSTREET, RESALE PRICE MAINTENANCE: ECONOMIC THEORIES AND EMPIRICAL EVIDENCE at 39 n.1. It follows that this Court's observation in the horizontal restraint context is equally applicable to

vertical agreements: "Not all arrangements . . . that have an impact on price are *per se* violations of the Sherman Act or even unreasonable restraints." *Broadcast Music, Inc.* v. *Columbia Broadcasting System*, 441 U.S. at 23.

2. *Intrabrand Competition.* Free rider termination removes an inefficient form of intrabrand competition—competition based on the free rider's lack of provision for services at the expense of the full service dealer—but it does nothing to lessen other efficient forms of intrabrand competition. Terminating a free rider leaves the door open for established full service dealers to compete with each other on both price and nonprice terms, and for new dealers to enter the market.[6]

Insofar as dealers may offer different styles or types of services, or be able to provide the same service at a lower cost, they will be able to shade prices and stimulate intrabrand price competition. That price competition, however, focuses on dealers' efficiency in providing necessary services, and not on mere free riding on services provided by others. Alternatively, dealers may compete on nonprice terms, increasing "the provision of point-of-sales services . . . to engross as much as possible of the difference between the retail price . . . and the (old) cost of distribution[,] spending more and more money on nonprice competition until the marginal cost of distribution has risen to meet the [dealer's] price." Posner, *Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions*, 75 COLUM. L. REV. 282, 284 (1975). *See also Valley Liquors, Inc.* v. *Renfield Importers, Ltd.*, 678 F.2d 742, 745 (7th Cir. 1982) (noting that "[t]he elimination of a price cutter who is taking a free ride on the promotional efforts of competing distributors will tend to stimulate nonprice competition among the distributors").

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6. In fact, free rider termination may for these reasons be considerably less restrictive of intrabrand competition than dealer location arrangements of the sort to which this Court applied the rule of reason in *Sylvania*. If one assumes limited end user mobility, a dealer location restriction may create a local monopoly and leave at least some dealers without *any* intrabrand competition whatsoever.

NOMDA concludes that, since an agreement to terminate a free rider has tangible efficiency-enhancing effects and stimulates intrabrand and interbrand competition, it is not the economic equivalent of a naked agreement to fix prices, and it does not thereby restrict dealer price flexibility. Such agreement to terminate a free rider shares none of the economic characteristics or effects that have led this Court to hold various agreements unlawful *per se*. NOMDA therefore urges this Court to affirm the court of appeals' conclusion that an agreement to terminate a free rider belongs to the only other category of vertical restrictions identified in *Monsanto*—"concerted action on nonprice restrictions," 465 U.S. at 761—and that these agreements must be analyzed under the rule of reason.

Responsible dealers would welcome a decision in this case recognizing that their provision of services is essential to the efficient operation of the distribution system, with benefits for manufacturers and end users alike. Because dealers cannot long continue to offer pre-sale, point-of-sale and post-sale services in markets in which free riders operate and profit at their expense, this Court should act in this case to protect the integrity of the distribution system by preserving the discretion of manufacturers to terminate free riders.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted,

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No. 85-1910

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF FOR THE CONSUMER ELECTRONICS GROUP OF THE ELECTRONIC INDUSTRIES ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF AFFIRMANCE

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November 6, 1987

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QUESTION PRESENTED

Whether it should be *per se* illegal for a manufacturer to agree with a full-service distributor to terminate another distributor who does not provide services as a means of preserving the viability of the full-service distrbutor and assuring that vital services associated with the product will continue to be offered.

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TABLE OF AUTHORITIES

Cases:

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INTEREST OF AMICUS CURIAE

The Consumer Electronics Group of the Electronics Industries Association ("EIA/CEG") a trade association that represents most manufacturers of audio, video and home information equipment, files this amicus curiae brief in support of Respondent.[1] The manufacturers repre-

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[1] Pursuant to Rule 36.1 of this Court, consent to the filing of this brief has been granted by both parties. Their consents have been filed with the Clerk.

sented by EIA/CEG have networks of distributors and retail dealers [2] who, through their sales efforts, determine a product's market penetration and shape consumers' views of a manufacturer.

With more than 50 brands of televisions and 50 brands of VCRs being sold, manufacturers need every competitive tool available to fight for market share in an intensely competitive marketplace. Imposition of a *per se* rule affecting distribution of a product restricts a manufacturer from a range of options—many of which enhance efficiency. Because this Court's decision in the present case will have a substantial impact on whether manufacturer's can take action imposing non-price vertical restraints which are often desirable in distributing products, it is of substantial concern to the *amicus curiae*.[3]

STATEMENT

1. In 1973, Sharp Electronics Corporation ("Sharp") terminated one of two Houston dealers carrying its electronic calculators, Business Electronics Corporation ("BEC"). BEC had been appointed the sole Houston distributor of Sharp calculators in 1968. Tr. 58-59. BEC, however, proved to be ineffective at stimulating sales. By 1972, it had fallen well behind the sales quotas Sharp had set. Defendant's Trial Exhibit No. 26. Sharp therefore decided to terminate BEC's dealership, Tr. 827-830, 700, and agreed to replace BEC with Gilbert Hartwell, Tr. 321-324. Hartwell was a full-service dealer who offered

[2] The terms "distributor(s)" and "dealer(s)" are used interchangeably through this brief as some manufacturers use a two-step distribution process—going through distributors, while others go directly to retail dealers.

[3] This *amicus curiae* brief represents the consensus view of the diverse membership of EIA/CEG. It should not be construed as having been submitted on behalf of or representing the views of any individual company.

a range of costly presale advertising, information and demonstration services. Tr. 343-344, 1031, 1102-1103. Sharp believed that in a market in which there was fierce interbrand competition, Tr. 931, Hartwell would be more effective than BEC in familiarizing consumers with Sharp's new, complex and expensive electronic calculators.

Though Hartwell had been assured he would have the exclusive Houston dealership in Sharp calculators, Tr. 322-324, there was some delay in terminating BEC. Tr. 1307-1308. With Hartwell's full-service dealership now operating in the same market, BEC took the opportunity to free-ride on Hartwell's services. Dispensing even with the few services that it had previously offered, BEC began to divert customers who had been persuaded to buy Sharp calculators through Hartwell's efforts, simply by distributing fliers offering the calculators at lower prices —prices Hartwell could not match if he was to cover the cost of providing the services necessary to educate customers about the merits of Sharp products. Tr. 110; 279-280; 283-284; 343-344; 346-348.

Hartwell complained about BEC's free-riding to Sharp. Tr. 249-280. He complained not about BEC's discounted prices as such, but about BEC's diversion of buyers: "We did all the legwork, all the selling and one little piece of flier came in and (the customer was) ready to buy the same product from (BEC)." Tr. 347-348. Eventually, in June 1973 Hartwell told Sharp that he would cease to sell Sharp calculators unless BEC was terminated within 30 days. Tr. 367-372; 420; 441. Sharp responded by terminating BEC. Tr. 371-374; 774-775; 867; 1309.

2. BEC then brought suit, alleging that Sharp's termination of BEC was pursuant to a price-fixing agreement illegal under the Sherman Act. The district court instructed the jury that it should find Sharp liable if it had agreed with Hartwell to terminate BEC because of BEC's

price cutting. J.A. 18. The jury returned a verdict for $600,000 in favor of BEC.

On appeal, the Fifth Circuit reversed, holding that the termination of a price cutter is not *per se* illegal unless it occurs as part of an agreement with a dealer to "set its prices at some level." Pet. App. 14a. In other words, "(t)he distributor cannot retain complete freedom to set whatever price it chooses." *Ibid.* The Court stated that this rule is necessary if manufacturers are to have flexibility to structure and adjust their distribution networks to achieve maximum efficiency. Citing this Court's concern in *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), that "legitimate conduct on the part of the manufacturers and distributors would not be penalized due to the ambiguity of . . . legal rule(s)," Pet. App. 11a, the Fifth Circuit upheld the freedom of manufacturers to terminate dealers in order to further legitimate nonprice goals such as preventing free-riding on presale services. The Fifth Circuit rejected alternative approaches that require a jury to determine whether a manufacturer's motives in terminating a price cutter are to reduce price competition or to protect distributors from free-riders, stating that a rule under which a manufacturer's "antitrust liability turned solely on a jury's guess as to the manufacturer's motivation" would deter legitimate manufacturer action. Pet. App. 12a.

SUMMARY OF ARGUMENT

A.

A manufacturer which has researched a market, identified a demand and developed a product to meet that demand has an important interest in structuring the distribution network through which its product will be marketed, and in ensuring that dealers in that network use the most appropriate and effective methods available to market the product. For many products, marketing is most effective when retailers offer prospective purchasers

a high level of pre-sale and post-sale services, educating the customer about the product, demonstrating its capabilities, and exploring with the customer whether the product meets his or her needs. *See Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 54-56 (1977). This sales method is particularly important for products new to the market and unfamiliar to consumers, and in general for any complex product where consumer satisfaction depends on understanding the product before making a purchase. The provision of pre-sale and other services increases sales, enhances consumer satisfaction and creates manufacturer goodwill. Manufacturers often require that their distributors and dealers provide these services.

Pre-sale and other services are often costly for distributors and dealers to provide. Free-riders may rely on full-service dealers to educate customers and persuade them to buy a product, and then divert the sale from the full-service dealer by offering the product at a lower price. Free-riders can charge less because they do not need to include in their price any amount covering the services that produced the sale—services that were provided by another dealer. In a market where free-riders operate, costly dealer-provided services soon disappear, as dealers are forced to drop them in order to compete on price. To ensure effective marketing of its products, a manufacturer must be able to exercise a reasonable degree of control over the methods used by its distributors. In particular, if it is to ensure that dealers offer the most effective mix of services, a manufacturer must be able to prevent free-riders from disrupting its distribution system.

B.

The fact is that virtually every vertical restraint affects product price. Servicing requirements, sales training, product promotion, all contribute to dealer costs and thus product price. A manufacturer should be able to impose

dealer requirements in any event, even though they indirectly affect price.

A manufacturer is hampered in dealing with free-riders however, by ambiguous legal rules that leave it uncertain of the legality of proposed courses of action. Manufacturers require unambiguous legal rules that establish clearly what agreements with dealers are illegal *per se* under the Sherman Act. Otherwise, the threat of treble-damage liability will deter manufacturers from action that would make for more effective marketing—and for more vigorous competition in the marketplace.

The rule applied by the Third Circuit in *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979), fails to provide manufacturers with meaningful guidance on the scope of *per se* illegality under the Sherman Act. Under the *Cernuto* rule, a jury may conclude that a manufacturer entered into an illegal price-fixing agreement if it finds that the agreement was motivated by a desire to restrain prices. Many perfectly legitimate nonprice agreements have an indirect impact on prices, and a rule under which treble-damage liability depends on a jury's ability to tell whether a manufacturer's action was motivated by a price effect or by a legitimate non-price objective is bound to chill legitimate manufacturer action.

The rule applied by the Court of Appeals in this case, on the other hand, follows in the tradition of *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), in reducing legal uncertainty concerning Sherman Act liability. The Fifth Circuit held that only agreements requiring a dealer to "set its prices at some level"—that is, agreements restraining a dealer's price flexibility in some way—are *per se* illegal. Pet. App. 14a. Under this rule, manufacturers have a clear guideline to follow in structuring their relations with distributors, and can react to the entry of free-riders into the market.

In short, agreements to set price are and should be *per se* illegal. Agreements which merely affect prices should be evaluated on their competitive effects.

ARGUMENT

A. Manufacturers Must Be Able to Set Minimum Non-Price Standards For The Distribution of Their Product

The rational development of legal rules to implement the Sherman Act prohibition on agreements in restraint of trade depends on an understanding of business realities. A rational definition of vertical price-fixing agreements that are illegal *per se* under the Act depends, in particular, on an understanding of the manufacturer/dealer relationship, and of the manufacturer's need to shape the way in which dealers market its products.

Most manufacturers of consumer products must rely on a network of independent distributors to bring their products to the public. Experience has shown that the manner in which distributors carry out this task has a great impact on consumer perceptions of the manufacturer's products, on the sales levels those products achieve, and on manufacturer goodwill. Consumer goods suppliers know that sales potential is less important to marketplace success than the sales efforts of independent distributors.

The type of distribution network that will maximize a product's market penetration naturally varies from product to product. Similarly, the sales methods that will be most effective vary with the nature of the product and the market-segment at which it is aimed. The manufacturer, who has studied the market, identified a demand and developed a product to satisfy that demand is in the best position to know what sort of distribution network and what sort of sales methods will maximize the impact of its product in the marketplace.

A manufacturer generally has a number of policies regarding dealer promotion of its products. For some products, effective marketing requires that retailers provide consumers with a high level of presale service. *See Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 54-56 (1977). A manufacturer that has developed a new

type of product may require retailers to provide potential customers with information about the product's function and capabilities, in order to educate consumers. Or a manufacturer that believes its product has significant advantages over its competitors may require the retailer to incur the expense necessary to train a staff which can explain and demonstrate those advantages.

A simple example illustrates the great importance of presale services. With the rapid development of video and audio technology, VCRs and compact disc players are manufactured with a wide range of features. Consumers may not understand the model differences unless the retailer explains and demonstrates those differences. For VCRs, the seller must explain to consumers the differences between machines with two or four heads, the effect of various kinds of circuitry, the operation of programming or editing features, and the various formats available. Only then can the consumer make an informed purchasing decision, and only then can a manufacturer be sure that its VCR has been properly understood and evaluated by the prospective purchaser, and weighed on its merits against its competitors.

There are many other ways in which a retailer's efforts affect a product's success in the market place. A manufacturer may wish to ensure that retailers carry a broad line of products, maintain sufficient stock to be able to meet orders quickly, provide an attractive and spacious shopping environment, offer prompt delivery and installation, or maintain facilities to repair products the retailer has sold. All or some combination of these retailer services may increase a product's sales, enhance consumer satisfaction, and invigorate competition. *See Sylvania*, *supra*, 433 U.S. at 54-55. It is vital, therefore, that manufacturers be able to supervise the operations of dealers, and control how a product is presented to potential purchasers.

Innovative manufacturers require flexibility. When certain activity is labeled *per se* illegal—manufacturers are by definition precluded from even explaining how their actions may improve efficiency and competition.

A manufacturer concerned with the integrity and effectiveness of its distribution network must be able to prevent disruption of that network by free-riding retailers. The sales methods that manufacturers desire retailers to use often involve significant initial investment and recurring expense for the retailers which must be recovered in the prices retailers charge their customers. Continued provision of necessary services is endangered if some retailers free-ride on services others have provided. This occurs when a full-service retailer informs the customer about a product and persuades the customer that the product fits his or her needs, but then loses the sale to a retailer who is able to offer the product for a lower price because it offers few or no services. Free-riders divert customers from retailers whose services—provided at substantial expense—have in effect "made the sale." Naturally enough, it is the full-service dealers who are a manufacturer's best source of information about the arrival of free-riders in the area. As the *Monsanto* Court recognizes, complaints from full-service dealers are a common element in business life.

Full-service dealers cannot afford to subsidize free-riders by offering costly services. Thus, in a market where free-riders operate, retailer-provided services can rapidly disappear. This can seriously injure a manufacturer dependent on retailer services to market its product effectively. Such manufacturers must be able to protect their full-service retailers from free-riders in order to keep their distribution systems efficient and to compete vigorously with rival manufacturers.

B. The Rule Applied By The Court Of Appeals Sets The Proper Balance Between Allowing Manufacturers Control Of The Distribution Of Their Product Without Allowing Control Of The Price Of The Product

For the reasons just discussed, a manufacturer must be able to exercise reasonable supervision over its distribution system to ensure efficient marketing of its products. And it is of vital importance that a manufacturer attempting to supervise its distribution network have the guidance of clear legal rules. Without bright-line rules establishing which dealer agreements are illegal, manufacturers may be reluctant to terminate inefficient dealers in ways which would enhance efficiency and strengthen competition. Manufacturers are deterred from making such adjustments by the threat of expensive lawsuits alleging an illegal agreement to fix prices. Without clear rules defining price-fixing agreements, the outcome of such lawsuits is difficult to predict and they may well result in treble-damage liability.

This Court is well-aware of the need for clear legal rules in this area, having recently stated that "it is of considerable importance that . . . concerted action on nonprice restrictions . . . be distinguished from price-fixing agreements, since under present law the latter are subject to *per se* treatment and treble damages." *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 763 (1984). The amicus wishes to stress, however, that the harm caused by a lack of clear rules identifying *per se* illegal agreements does not stop with the unpredictable imposition of treble-damage liability. Rather, the harm extends to the perpetuation of inefficient sales practices, such as free-riding on another dealer's services, which disrupt distribution systems and dampen market competition.

In *Monsanto*, this Court acted to protect manufacturers from uncertainty created by the possibility that price-fixing agreements might be inferred from highly ambiguous evidence. In the present case, the Court has the opportunity to protect manufacturers from the uncertainty that follows from any definition of price-fixing that invites a jury to guess the manufacturer's motives in entering an agreement.

The rule applied by the Fifth Circuit in this case brings welcome and indeed essential certainty to the manufacturer-distributor relations, by making it clear that only agreements that restrict the dealer's price flexibility in some way are *per se* illegal. Pet. App. 14a. Under this definition, a manufacturers knows with certainty that agreements to protect dealers from free-riders and thereby achieve goals such as the continued provision of services to consumers will be treated by the courts under the rule of reason, and not under *per se* rules.

The Fifth Circuit properly rejected the definition of vertical price-fixing adopted by the Third Circuit in *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979). Under *Cernuto*, a manufacturer faces the prospect of treble-damage liability simply because an adjustment to distribution network has an indirect impact on price, even though the adjustment was undertaken in order to prevent free-riding on full-service dealers and even though it involves no agreement that restricts a dealer's flexibility in setting its prices. Such liability may be imposed if a jury decides that an overtly nonprice agreement having an indirect price impact was in fact *motivated* by a desire "to restrain price movements." *Id.* at 168-169. The *Cernuto* rule creates enormous uncertainty because "(a)ny vertical non-price restriction may affect resale prices," including any legitimate restriction. Pet. App. 9a. As a result, the rule leaves the manufacturer's fate dependent on a jury's ability accurately to psychoanalyze the manufacturer's motives to determine whether the inevitable price impact of an agreement was the agreement's purpose or merely its incidental consequence. As Judge Posner has accu-

rately noted, "(t)here is . . . a certain unreality in the careful parsing of motives that *Cernuto* seems to require." *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 744 (7th Cir. 1982).[4]

The chilling effect on manufacturers of such an amorphous psychological inquiry cannot be overestimated. The Fifth Circuit correctly stated the problem: "the manufacturer which desires to terminate a price cutter because of its free riding will be deterred from this legitimate action because it is indistinguishable, except perhaps to a mind reader, from what *Cernuto* prohibits, *i.e.*, termination of a price cutter because of its price cutting." Pet. App. 12a. As Judge Jones cogently remarked, "(s)emantic nuances are costly to businessmen in the real world," Pet. App. 22a—particularly, we would add, when these nuances are directed at juries.

What is costly to businessmen will be costly to consumers. The uncertainty generated by *Cernuto's* semantic nuances results in serious inefficiency costs to manufacturers attempting to organize and oversee the operation of an effective distribution system. These costs are of necessity passed on to the ultimate purchaser in the form

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[4] Judge Posner continued (*ibid.*):

> "If a supplier wants his distributors to emphasize nonprice rather than price competition, which . . . is the usual reason why he would restrict his distribution, he will be hostile to price cutters because they will make it harder for his other distributors to recoup the expenditures that he wants them to make on presale services to consumers and on other forms of nonprice competition, and of course the undersold distributors will be equally or more hostile. The motive of supplier and distributors alike could thus be described as wanting to eliminate price cutters yet there would be no *per se* illegality so long as the supplier was not just knuckling under to the distributors' desire for less competition. It is difficult to see how a court could distinguish empirically between such a case and the pure antipathy to price competition envisaged by *Cernuto*."

of higher prices. Thus, it is the consumer—the intended beneficiary of the Sherman Act—who in the final analysis has most to gain from the certainty provided by the Fifth Circuit's rule in this case.

CONCLUSION

The judgment of the Court of Appeals should be affirmed.

Respectfully submitted,

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APPENDIX A

ELECTRONIC INDUSTRIES ASSOCIATION
CONSUMER ELECTRONICS GROUP
MEMBERSHIP
OCTOBER, 1987

COMPANY
Allsop, Inc.
Ambico, Inc.
Ampex Corporation
AOC International
Arvin Electronics
Asti Nikko Technology Corp.
Atari Corporation
Audiovox Corp.
Audio Research Corp.
Audio Technica U.S., Inc.
Bang & Olufsen of America, Inc.
Barcus-Berry Electronics, Inc.
BASF Corp. Information Systems
Bib Audio/Video Products
Blaupunkt Div./Robt. Bosch Sales
Boston Acoustics, Inc.
Byte Resources Company
Canon U.S.A., Inc.
Canton
Casio, Inc.
Clarion Corp. of America
Cord Electronics Inc.
Curtis Mathes
Delco Electronics Corp.
Denon America, Inc.
Discovery Systems, Inc.
Dynascan Corp.
Eastman Kodak
Emerson Radio Corp./H.H. Scott

Epson America, Inc.
Finial Technology
Fisher Corporation
Fortel Corporation
Fox Marketing, Inc.
Fuji Photo Film USA, Inc.
GC Thorsen
General Electric Company
Goldstar Electronics International, Inc.
The David Hafler Company
Hitachi Sales Corp. of America
Home Information Systems
International Jensen
Jasco Products Co., Inc.
JBL, Inc./Harman Intl.
JVC Company of America
Kenwood Electronics
Kloss Video Corporation
Konica U.S.A., Inc.
Lebo Peerless Corporation
Madrigal, Ltd.
Magnepan, Inc.
Marantz Company, Inc.
Maxell Corporation
Memtek Products
Mitsubishi Electric Sales America, Inc.
Monster Cable Products, Inc.
Mura Corp.
N.A.P. Consumer Electronics Corp.
NEC Home Electronics (U.S.A.) Inc.
OKI America, Inc.
Ortofon, Inc.
Panasonic Company
Pfanstiehl
Pioneer Electronics (USA), Inc.
Polaroid Corporation
Polk Audio, Inc.
Quasar Company

Rabbit Systems, Inc.
Recoton Corporation
Royal Sound Company, Inc.
Samsung Electronics America, Inc.
Sansui Electronics Corp.
Sanyo Manufacturing Company
Scosche Industries
Sega of America, Inc.
Sharp Electronics Corp.
Shure Brothers, Inc.
Sima Products Corporation
Sony Corporation of America
Studer Revox America, Inc.
Tandberg of America, Inc.
Tandy Corporation
TDK Electronics Corp.
TEAC Corporation of America
Telequest, Inc.
3M Company
Toshiba America, Inc.
Triad Design, Inc.
Videonics Incorporated
Wells-Gardner Electronics Corp.
Xantech Corporation
Yamaha Electronics Corp. U.S.A.

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No. 85-1910

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

BUSINESS ELECTRONICS CORPORATION,
Petitioner,

v.

SHARP ELECTRONICS CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF OF THE NATIONAL ASSOCIATION OF MANUFACTURERS AS AMICUS CURIAE IN SUPPORT OF RESPONDENT

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QUESTION PRESENTED

Whether a manufacturer has engaged in an illegal conspiracy to fix resale prices simply because it has terminated a dealer following price-related complaints from a competing dealer.

Whether a price-cutting free-rider may be terminated by the manufacturer at the behest of a full-service dealer without action being regarded as a per se vertical "price-fixing" conspiracy.

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On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

---

BRIEF OF THE NATIONAL ASSOCIATION OF MANUFACTURERS AS AMICUS CURIAE IN SUPPORT OF RESPONDENT

This brief is filed on behalf of the National Association of Manufacturers in support of Respondent, Sharp Electronics Corporation ("Sharp"). Consent from counsel for both parties has been filed with the Clerk of this Court.

INTEREST OF THE AMICUS CURIAE

The National Association of Manufacturers of the United States of America ("NAM") is a non-profit voluntary business association incorporated under the laws of the State of New York. The NAM represents approxi-

mately 13,000 companies, large and small, located in every state of the Union. Further, the NAM is affiliated with an additional 158,000 businesses through the Associations Council and the National Industrial Council. The membership of the NAM represents an estimated 80 percent of all goods manufactured in the United States.

As the principal representative of America's manufacturing community, the NAM has had a long and substantial interest in matters relating to the distribution and marketing of manufactured products. It believes that efficient operation of our large national economy requires that rules regulating trade be clear, predictable, and economically rational, and that they be consistently applied by government enforcers and courts.

Thus, the ramifications of particular antitrust decisions may extend far beyond the parties and strike at the heart of our competitive national economy.

The vast majority of NAM members are subject to the jurisdiction of the federal antitrust laws. As active participants in the free-market system of the United States, NAM's members have a vital interest that these laws be interpreted according to consistent and predictable standards and in ways which enhance business efficiency and consumer welfare.

STATEMENT

Sharp is a supplier of various consumer and business products, including calculators, and distributes these products through retail dealers. During the period prior to this suit, Sharp wanted its dealers to emphasize pre-sale educational and promotional services in order to stimulate interest and demand, and provided them with suggested resale price lists. One of its dealers in the Houston area, Petitioner Business Electronics Corporation ("BEC"), often sold at prices lower than those on Sharp's suggested retail price list.

In 1972, due to BEC's inability to meet its sales quotas, Sharp appointed Gilbert Hartwell as a second dealer in the Houston area. Hartwell was a full-service dealer, with an extensive advertising program and a trained sales staff that demonstrated and discussed Sharp products with prospective customers. After Hartwell's appointment, BEC dispensed with advertising and its sales force, while undercutting Hartwell's prices.

Hartwell was justifiably concerned that he did not have an exclusive dealership in the Houston area, as he had expected, and he complained to Sharp. In addition, he complained that BEC was able to free ride on his investment in product promotion and other sales-related services. Hartwell presented a "him or me" ultimatum to Sharp, and Sharp was forced to choose between giving an exclusive territory to Hartwell or, by operation of the ultimatum, give up Hartwell's business and sell through BEC. Sharp chose Hartwell, and was sued by BEC.

At no time did Sharp require compliance by either Hartwell or BEC with its suggested retail price list. In fact, Hartwell complained that all he ever heard from Sharp was "the same broken record, that a manufacturer could not tell a dealer what to sell his product for . . . [n]o matter who I talked to . . . I heard that over and over." Moreover, Hartwell himself did not always adhere to Sharp's suggested retail prices.

Nevertheless, the trial judge instructed the jury to find a per se violation of the Sherman Act if it found an understanding between Hartwell and Sharp to terminate BEC "because of" BEC's price cutting. On appeal, the Fifth Circuit ruled that a manufacturer that terminates a price-cutting distributor following complaints from a competing distributor is not per se liable for illegal price fixing unless there is proof of an agreement on price between the manufacturer and the competing distributor. It reversed a jury verdict for BEC, and remanded the case for further deliberations under this standard.

The Fifth Circuit, rejecting an alternative rule,[1] held that

> An agreement to terminate a price cutter does not fix prices at any specific or general level but merely frees the complaining dealer to set prices as he chooses . . . . [I]n order for a manufacturer's termination of a distributor to be illegal *per se*, it must be pursuant to a price maintenance agreement with another distributor. That distributor must expressly or impliedly agree to set its prices at some level, though not a specific one. The distributor cannot retain complete freedom to set whatever price it chooses.

780 F.2d at 1216 & 1218.

The writ of *certiorari* was issued to review this decision of the Court of Appeals for the Fifth Circuit. Petitions in other cases are currently pending before this Court, awaiting the outcome of this case.[2]

SUMMARY OF THE ARGUMENT

As a result of *Sylvania*[3] and its progeny, a manufacturer facing interbrand competition has substantial flexibility in developing effective dealer arrangements which can pass muster on the fact-based antitrust rule of reason. Still a manufacturer cannot enter into an "agreement" with a dealer which can be properly characterized as "price fixing" or "price maintaining" without offending a long-established per se prohibition. This Court's 1984 decision in *Monsanto*[4] substantially clarified the "agreement" issue, but was less precise on the "price fixing" issue. The "price fixing" characterization question is a vital one because (i) every discontinued dealer will make a "price fixing" allegation in order to obtain the advantage of a per se rule, and (ii) almost every important distribution activity required by a manufacturer under *Sylvania* has cost, and hence "price" implications.

[1] Business Elecs. Corp. v. Sharp Elecs. Corp., 780 F.2d 1212, 1216 (5th Cir. 1986).

[2] McCabe's Furniture, Inc. v. La-Z-Boy Chair Co., 798 F.2d 323 (8th Cir.), *petition for cert. filed*, 55 U.S.L.W. 3495 (U.S. Dec. 29, 1986) (No. 86-1101); Garment Dist., Inc. v. Belk Stores Serv., Inc., 799 F.2d 905 (4th Cir.), *petition for cert. filed*, 55 U.S.L.W. 3394 (U.S. Nov. 17, 1986) (No. 86-794).

[3] Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977).

[4] Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984).

The ability of a manufacturer to terminate a dealer in order to improve its distribution is important to an efficient, competitive economy. Any dealer termination is an important decision which may go to the heart of a manufacturer's ability to market its products.

In truth, a manufacturer and its distributors are essentially joint venturers in marketing the manufacturer's product. Dealers that fail to carry out education and promotion activities have an inherent advantage over those that do not. They may become "free riders" on the services provided by the full service dealer, making sales to customers who have already been educated and convinced about the product by the full service dealer. This "free rider" problem is obviously of great concern to both a manufacturer and its dealers. Success of their common enterprise necessarily requires communication about the joint marketing program, which may include discussion of non-performance by a competing distributor to the detriment of the overall program.

Concern about compliance with the service aspects of a manufacturer-distributor arrangement is entirely legitimate and cannot properly be viewed as simply an adjunct to vertical "price fixing." Yet performance of legitimate distribution services cannot be entirely separated from pricing. As this Court stressed in *Sylvania*, "[p]er se rules of illegality are appropriate only when they relate to conduct that is manifestly anticompetitive."

A terminated "free rider" should not be entitled to get to a jury on a "price fixing" theory simply because a

price-related complaint preceded termination. Therefore, the operative legal standard must separate those cases in which a manufacturer acts out of a legitimate concern over the performance of distributors, and thus promotes competition, from cases where its ends are illegitimate. The standard must provide concrete guidance for a fact-finder, and thus preclude speculation based upon often ambiguous evidence.

ARGUMENT

I. MANUFACTURERS REQUIRE A CLEAR AND CONSISTENTLY APPLIED LEGAL RULE TO DEAL WITH THE RECURRING SITUATION TYPIFIED BY THIS CASE.

The NAM filed an amicus brief in this Court over four years ago in *Monsanto Company v. Spray-Rite Service Corporation*, 465 U.S. 752 (1984), asking this Court to articulate (1) a clear legal standard to determine when a dealer termination case is to be submitted to the jury and (2) a more structured jury inquiry when it is. In *Monsanto*, this Court said unanimously that there were two characteristic questions in a dealer termination case of this general variety: (1) "the basic distinction between concerted and independent action," and (2) the "important distinction . . . between concerted action to set prices and concerted action on nonprice restrictions." 465 U.S. at 761. The main thrust of the Court's decision was on the first question, but the Court reached some conclusions which are important to the second.

It ruled that the existence of a conspiracy to maintain resale price levels under Section 1 of the Sherman Act cannot be inferred simply from evidence that a manufacturer terminated a price-cutting distributor following the receipt of complaints from other distributors concerning the price cutting. Instead, there must be direct or circumstantial evidence that tends to prove that the manufacturer and others had a conscious commitment to a common scheme designed to achieve the unlawful objective of fixing prices. 465 U.S. at 764. The Court thus addressed the fundamental need of manufacturers for clarity in this area.

The ability of a manufacturer to terminate a dealer in order to improve its distribution is important to an efficient, competitive economy. Any dealer termination is an important decision which may go to the heart of a manufacturer's ability to market his products. Such decisions are never taken lightly, particularly in a legal climate that subjects manufacturers to potential liability because another dealer has complained. Any antitrust challenge to a manufacturer's decision to terminate a distributor must recognize the legitimate needs of a manufacturer and its distributors to constantly communicate with one another about marketing. It is perfectly appropriate to exchange information about prices and how the products are being received in the market. A manufacturer is properly concerned that any marketing programs it adopts be properly funded by dealers that must implement them, and that free riders do not interfere. 465 U.S. at 762-63. This is especially true if a product is complex, potentially harmful, new, or generally unknown, since a great deal of labor-intensive promotion and educational activities have to be developed and implemented just to properly display the product.[5] Such an effort requires continuous communication between the manufacturer and its individual distributors and dealers.

Dealers that fail to carry out education and promotion activities have an inherent cost advantage over those that do not. They may become "free riders" on the services provided by the full service dealer, making sales to custom-

[5] Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 54-55 (1977); Isaksen v. Vermont Castings, Inc., 825 F.2d 1158, 1161 (7th Cir. 1987).

ers who have already been educated and convinced about the product by the full service dealer. *See Sylvania*, 433 U.S. at 55. The distributors who provide the service are placed at a cost disadvantage vis-a-vis the distributor who does not, and the non-complying distributor can reduce prices accordingly. As a result, promotional and educational "services might not be provided by retailers in a purely competitive situation, despite the fact that each retailer's benefit would be greater if all provided the services than if none did." 433 U.S. at 55. This problem, which can apply equally at the distributor level, is particularly acute where (as in this case) distributors are not given exclusive territories.

This free rider problem is obviously of great concern to both a manufacturer and its distributors. Not surprisingly, it is frequently an aspect of ongoing discussions between them. Where a distributor cuts prices sharply, a competing distributor is likely to complain to the manufacturer. A manufacturer has no control over such complaints, and the complaints do not indicate any illegal concerted action. 465 U.S. at 763. Moreover, a manufacturer who assumes greater responsibility for distributor planning is more likely to receive such complaints in the normal course of business. Thus, it is ironic that a manufacturer that is most active in making his product as competitive as possible by monitoring market conditions and by providing educational and promotional materials and services through distributors is also most likely to be sued for an antitrust violation when those distributors provide feedback on the marketplace.[6]

Because communications between a manufacturer and its distributors are important to the success of the com-

[6] The antitrust laws are designed to encourage, not discourage, discussions between manufacturers and distributors on the most effective mechanisms for increasing sales. *See* Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752, 764 (1984); Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc., 824 F.2d 582, 593 (8th Cir. 1987).

mon enterprise, manufacturers have a vital interest in maintaining good relations with distributors. Thus, negative feedback about price-cutting distributors is likely to trigger an analysis by the manufacturer of whether the price cutting is indicative of a failure to provide sales and educational services. If a distributor is failing in his non-price related obligations, a manufacturer has a legitimate interest in terminating the distributor.

That legitimate interest is intensified when a competing distributor not only complains about the price cutter, but also threatens to terminate his own activities on behalf of the manufacturer. Such a threat gives the manufacturer a Hobson's choice: it must terminate the discount distributor and be subject to suit for "agreeing" with the other distributor to fix prices, or it must be prepared to relinquish the full service distributor, along with the educational and promotional services it provides. If the manufacturer keeps the discount distributor, despite that distributor's failure to comply with contractual obligations, the business that is generated from the full-service educational and promotional program is lost to the substantial detriment of the consumer.

In this situation, it is imperative that this Court delineate a clear set of principles that must be applied. The termination of a dealer following complaints about his prices does not raise an inference of a per se illegal price fixing conspiracy. *Monsanto*, 465 U.S. at 764. Evidence relating to the business justification for a termination is essential to consider.[7] The extent to which remaining

[7] Indeed, there may be a variety of business reasons totally unrelated to price for terminating a free rider, including tax considerations, avoiding mail-order transactions or transshipping, reducing the number of distributors, and avoiding credit problems. Valley Liquors, Inc. v. Renfield Importers, Ltd., 822 F.2d 656, 663-64 (7th Cir. 1987); Beach v. Viking Sewing Mach. Co., 784 F.2d 746, 750 (6th Cir. 1986); O.S.C. Corp. v. Apple Computer, Inc., 792 F.2d 1464, 1468 (9th Cir. 1986).

dealers alone decide the prices at which they sell is crucial.[8] Juries must be given all the facts and must not be called upon to draw adverse inferences of conspiracy from acts that a manufacturer would do even without having received complaints from another dealer.

II. DEALER COMPLAINTS ABOUT ANOTHER DEALER'S PRICING DO NOT, WITHOUT MORE, CONVERT A DEALER TERMINATION CASE INTO A "PRICE-FIXING" CASE.

Neither party disputes the fact that Sharp may not force a dealer to sell all Sharp calculators at a particular fixed price. Such an agreement takes away the dealer's ability to make independent pricing decisions, preventing him from taking into account the severity of competition in the calculator market, the cost of his sales and promotional activities, and the size of the profit he wants to make. Whether such an agreement is illegal per se[9] or judged under the rule of reason[10] is not the principal issue before the Court, and NAM has taken no position on this issue.

At the other end of the spectrum, neither party disputes that a manufacturer who has received *no* complaints from other dealers may terminate a distributor arrangement with a dealer if the dealer is failing to perform legal contractual obligations under a binding contract.

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[8] AAA Liquors, Inc. v. Joseph E. Seagram and Sons, Inc., 705 F.2d 1203, 1205-06 (10th Cir. 1982), *cert. denied*, 461 U.S. 919 (1983); Chisholm Brothers Farm Equipment Co. v. International Harvester Co., 498 F.2d 1137, 1142 (9th Cir.), *cert. denied*, 419 U.S. 1023 (1974).

[9] Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373, 408 (1911); O.S.C. Corp. v. Apple Computer, Inc., 792 F.2d 1464, 1467 (9th Cir. 1986).

[10] Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc., 824 F.2d 582, 593 (8th Cir. 1987).

This principle, the *Colgate* doctrine,[11] is essential to marketing flexibility, competitiveness, and, indeed, the freedom inherent in the American free enterprise system.

Somewhere in between these principles lies the *Sharp* case. Had there been no complaints from Hartwell, BEC would never have filed suit, much less be before this Court. Had Hartwell refused to accept a nonexclusive dealership agreement from the beginning, Sharp would have been within its rights to terminate BEC and grant the equivalent of an exclusive distributorship to Hartwell. If BEC had refused to provide manufacturer-required warranty service on calculators it sold, resulting in customers coming to Hartwell for servicing of calculators he did not sell, Hartwell could have complained and Sharp could have terminated BEC.

Because Hartwell complained about discounting by BEC, the spectre of resale price maintenance was raised. Was Sharp terminating BEC because Sharp wanted BEC to perform point-of-sale and other promotional services? Or was the termination part of an agreement between Sharp and Hartwell to keep prices high? If BEC had been selling at full suggested retail prices, and Hartwell issued a "him or me" ultimatum to Sharp, would Sharp have been liable for resale price maintenance for terminating BEC?

When one dealer complains to a manufacturer about another dealer's prices, alarms go off. American manufacturers are extremely sensitive to the state of the law regarding resale price maintenance, the risks of terminating dealers, and the viscissitudes of judges and juries. Indeed, Sharp did everything short of terminating Hartwell to emphasize its inability to require, coerce, or otherwise convince a dealer to abide by its suggested retail prices. It was only when Hartwell's "him or me" ultimatum was presented that Sharp was forced to choose

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[11] *See* United States v. Colgate Co., 250 U.S. 300, 307 (1919) (a business generally has a right to deal, or refuse to deal, with whomever it likes, as long as it does so independently).

between competing dealers on the basis of all factual and legal factors.

Those factors involved the essence of managing a business of any kind. They involved deciding which of two or more alternatives would result in the most competitive product marketing capabilities, considering quality, quantity, efficiency, and compatibility with a marketing program. Sharp exercised its business judgment, and whether it was successful was to be tested in the harshness of the fiercely competitive world of calculators.

Applying to such judgments an additional level of scrutiny under the antitrust laws should be done only when the law is clear and the need for such scrutiny is founded on rational economic and competitive justifications. For an otherwise difficult business decision to be characterized as a price-fixing agreement, there must be evidence of just that. The stakes are high, for a wrong decision exposes a manufacturer to competitive punishment in the marketplace and legal punishment in court.

An agreement regarding price, without enforcement, is a practical nullity.[12] It is not an agreement on price at all, but rather is an exhortatory statement of preference that has no binding effect. A dealer may ignore it with impunity. Thus, the understanding between a manufacturer and a dealer on prices in resale price maintenance cases is crucial to a finding that there is a conspiracy. This Court has held that only when such an agreement is enforced by coercion or some other action by a manufacturer does it run afoul of the Sherman Act.[13]

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[12] *See* Dr. Miles, 220 U.S. 373, 406-08 (1911) (vertical price-fixing restrictions invalid and unenforceable).

[13] Monsanto, 465 U.S. at 764 n.9 (plaintiff must show that distributor conformed to suggested price and communicated its acquiescence or agreement, and that this was sought by the manufacturer); United States v. Parke, Davis & Co., 362 U.S. 29, 43 (1960). *See* Yentsch v. Texaco, Inc., 630 F.2d 46, 52 (2d Cir. 1980).

In this case, whether there was such coercion, undue influence or other action sufficient to constitute a conspiracy by Sharp is a question of fact that we are not qualified to resolve. Instead, we seek a reformulation by this Court of the analysis that must be utilized in trial courts to determine whether a conspiracy exists. *Monsanto* made it clear that dealer complaints about the prices of competing dealers are common, natural, unavoidable and legitimate, but at what point does a manufacturer become guilty of "price fixing" for terminating dealers about whom such complaints have been lodged?

Part of the problem is that "price fixing" conspiracy concepts developed in the horizontal competitor context are difficult to apply in the manufacturer-dealer context. Random discussions among direct competitors about prices are often suspect.[14] The question of whether chance contacts among competitors become a "conspiracy" depends on whether the alleged conspirators "had a unity of purpose or a common design and understanding, or a meeting of minds." *American Tobacco Co. v. United States*, 328 U.S. 781, 820 (1946).

In the manufacturer-distributor context, the parties plainly have "a unity of purpose or a common design" to develop an effective merchandising program. This is entirely legitimate. Non-performance of key duties of such a program by any participant is necessarily of concern to others. Pricing is part of the picture, because "free riding" by a non-performing distributor often involves price cutting. *Davis-Watkins Co. v. Service Merchandise*, 686 F.2d 1190, 1195 (6th Cir. 1982). Hence the inquiry cannot be simply whether the manufacturer and its distributors communicated and were concerned about price —but whether the actions taken were consistent with the legitimate goals of the manufacturer in establishing the

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[14] *See* A. Smith, The Wealth of Nations 170 (4th ed. 1789), *cited in* United States v. Realty Multi-List, Inc., 629 F.2d 1351, 1370 (5th Cir. 1980).

joint program. Only when communication and any resulting action are shown to be inconsistent with such legitimate goals is there evidence "sufficient to raise an inference of concerted action" and hence go to the jury.

It is clearly inappropriate to apply the "price fixing" label to such complaint-and-termination evidence, which is often economically ambiguous, without regard to the relationship of the communication and conduct to the manufacturer's legitimate goals. As this Court stressed in *Sylvania*, "[p]er se rules of illegality are appropriate only when they relate to conduct that is manifestly anticompetitive." [15] Even in the horizontal competitor context, the Court has stated recently that the inquiry is "whether the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output, and in what portion of the market, or instead one designed to 'increase economic efficiency and render markets more, rather than less, competitive.'" *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1, 19-20 (1979). It is very hard to say that communications between a manufacturer and its distributor about the implementation of a bona fide joint marketing program—or the nonimplementation of the marketing program by the competing distributor—are "manifestly anticompetitive" or "always or almost always tend to restrict competition and decrease output." This is especially so where (as in *Monsanto* and *Sylvania*) the marketing program was instituted by a manufacturer with a small market share and it proved successful in enhancing its competitive position.

Concern about compliance with the service aspects of a manufacturer-distributor arrangement is entirely legitimate and cannot properly be viewed as simply an adjunct to vertical "price fixing." Yet performance of legitimate

[15] 433 U.S. at 49-50, discussing the standard formulation in *Northern Pacific Railway Co. v. United States*, 356 U.S. 1, 5 (1958).

distribution services and resale price cannot be entirely separated.

Accordingly, this Court should specifically mandate structured judicial inquiry to govern the recurring complaint-and-termination case. In the light of *Sylvania* and its underlying policies, the focus should be on the vigor of the interbrand competition and the bona fides of the manufacturer's efforts.

The operative legal standard must separate those cases in which a manufacturer acts out of a legitimate concern over the performance of distributors, and thus promotes competition, from cases where its ends are illegitimate. The standard must provide concrete guidance for a fact-finder, and thus preclude speculation based upon often ambiguous evidence. We therefore respectfully suggest that the likelihood a manufacturer's purpose *could* reasonably have been to fix resale prices should be assessed before the jury is permitted to find a conspiracy. To that end, we respectfully suggest that a trial court should consider at least the following questions in determining whether a "conspiracy" claim in a complaint-and-termination case ought to be sent to the jury on a per se basis:

1. Was the manufacturer operating in a market where active interbrand competition existed or was there evidence of a general lack of uniformity in the resale prices of its products? [16]

2. Did the manufacturer have in place a program to improve its overall success in interbrand competition by imposing education, promotion or service responsibilities on its distributors?

[16] *See* National Marine Elec. Distribs., Inc. v. Raytheon Co., 778 F.2d 190, 193 (4th Cir. 1985); Valley Liquors, Inc. v. Renfield Importers, Ltd., 678 F.2d 742, 745 (7th Cir. 1982).

3. Did the manufacturer have a legitimate concern about the plaintiff's failure to satisfy its performance obligations or about other breaches of its distribution contract? [17]

If the answer to each of these questions is "yes," we respectfuly submit that the manufacturer's termination or non-renewal of the plaintiff does not become a "price-fixing conspiracy" simply because one or more competing distributors complained to the manufacturer about the plaintiff's pricing. Accordingly, it should not be submitted to the jury. Instead, for a case to withstand a motion for summary judgment, there must be some evidence that price was the *principal cause* of the termination, and that other legitimate reasons the manufacturer had are found to be either unsupportable pretexts or of insubstantial importance considered in light of any resale price maintenance motives.

Of course, requiring a plaintiff to prove that price alone was the principal cause of a dealer termination is a serious burden. But price fixing conspiracies, subject to treble damages and criminal penalties, are not to be taken lightly by the courts or by the litigants. Proving causation unambiguously is essential where distributor complaints about another distributor's prices are sometimes followed by termination for reasons firmly grounded in the distributor's failure to honor his service obligations.

The Fifth Circuit's ruling provides one way to prove that a termination was caused in fact by a resale price maintenance agreement. It requires proof that a distributor "expressly or impliedly agree[d] to set its prices at some level, though not a specific one. The distributor cannot retain complete freedom to set whatever price it chooses." 780 F.2d at 1218. The existence of a suggested retail price list is some evidence of this, but evidence

[17] *See* Valley Liquors, Inc. v. Renfield Importers, Ltd., 822 F.2d 656, 663-64 (7th Cir. 1987).

that the list is not enforced eviscerates the probative value of this evidence. The fact that a manufacturer has explained to a distributor its inability to enforce its suggested price list against other distributors is also evidence tending to disprove a price-fixing conspiracy. Indeed, if there is never any indication from the accused manufacturer that it has any intention of enforcing compliance in any way with its suggested price list, it would be unfair and unreasonable for this Court or any court to infer a conspiracy without clear evidence to the contrary.

CONCLUSION

This Court should take this opportunity to make the elements of proof in a case involving an allegation of resale price maintenance absolutely clear. Despite *Monsanto*'s unusual unanimity, the lower courts continue to deal with cases raising questions about this area of law, and both manufacturers and distributors suffer from the uncertainty. Affirmation of the decision below would provide all litigants with clear guidance.

Respectfully submitted,

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